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Delivering the Goods:

The Federal-Provincial Division of Spending Powers

Jean-Michel Cousineau,
Claude E. Forget,
and
John Richards

The Canada Round:
A Series on the Economics of
Constitutional Renewal — No. 12

John McCallum, Series Editor

C.D. Howe Institute

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Foreword

Canada appears poised to embark on an historic political reconfiguration. It is essential that this process be undertaken with a clear and widely diffused understanding of the well-spring of Canadians' economic prosperity.

It is with that in mind that the C.D. Howe Institute presents this series of monographs entitled *The Canada Round*. The series assembles the work of many of Canada's leading economic and political analysts. The monographs are organized into two groups. The first group, called "The Economics of Constitutional Renewal," rests on the assumption of renewed federalism and is organized around economic themes. It examines the economic goals that Canadians have set for themselves, as well as the means of achieving them and the influence of alternative constitutional structures.

The second group of studies, called "The Economics of the Breakup of Confederation," examines the economic consequences of Quebec independence for both Quebec and the rest of Canada. A unique feature of the "Breakup" studies is that they are integrated with the research that has already been carried out by Quebec's Bélanger-Campeau Commission. Where appropriate, each of the studies in this group includes a summary of the relevant analysis by the Bélanger-Campeau Commission, contributions by experts from across Canada, as well as shorter critiques or replies. This format, we believe, will help to pierce Canada's "several solitudes" and create a pan-Canadian meeting of minds.

The Canada Round is not intended to alarm or frighten — the process of collective political definition in this country will turn on more than simply questions of dollars and cents. And, as these monographs will reveal, economics rarely produces an open-and-shut case as to the superiority of one possible set of rules over another. Even if it could do this, it would be unwise to assume that economic analysis alone could change the minds of those who are already committed to a particular vision of the political future.

It is equally clear, however, that Canadians are now seeking a greater understanding of the links between the economy, the Constitution, and legal and political life. A significant reform of the Constitution will influence the economy, in some cases for the better; a rending of the Constitution under conditions of acrimony will almost certainly damage it. Thus, the purpose of the series is to help Canadians think constructively about the benefits and costs of alternative constitutional designs.

Underlying the series is a focus on the economic well-being of Canadians, now and in the future. To best insure this well-being over the short run, Canada needs calm, open negotiations in which efforts are made to understand and incorporate the aspirations of all the participants. This series of monographs is dedicated to that effort.

John McCallum, the series editor and Chairman of the Department of Economics at McGill University, organized the intellectual input. Within the C.D. Howe Institute, David Brown, Senior Policy Analyst, played a coordinating role. This twelfth monograph in the series was copy edited by Lenore d'Anjou, Margaret Hoogeveen, and Barry A. Norris, and desktop published by Brenda Palmer. As with all C.D. Howe Institute publications, the analysis and views presented here are the responsibility of the authors and do not necessarily reflect the opinions of the Institute's members or Board of Directors.

Thomas E. Kierans
President and
Chief Executive Officer

The Study in Brief

In his highly readable essay on the division of spending powers, John Richards begins with a historical overview of the subject. He turns next to a discussion of the relative merits of the centralization and decentralization of powers, and he ends with nine recommendations designed to provide what he sees as an appropriate division of powers, as well as a recipe for keeping the country together.

Richards' central theme is that social policy should be left mainly to strong provincial governments. If we must have a social charter, then let its scope be modest. This seemingly "right-wing" position runs directly counter to the "left-wing" position of those who call for a strong social charter and a strong central government with the capacity to impose national standards and to launch new national programs in areas such as child care. The novelty and strength of Richards' argument is that his is an attack "from the left." Himself a member of the New Democratic Party, Richards shares the social policy objectives of "charter nationalists," but he argues simply that their policies will not work.

Richards' argument can be summarized in three points. First, for various reasons, a neutral observer in the 1930s would have predicted a more rapid development of the welfare state in the United States than in Canada. Yet it was Canada, not the United States, that developed medicare. This, according to Richards, was because the provinces, unlike the states, had the power to experiment with approaches to social policy. Successful experiments, notably Saskatchewan's experience with medicare, were then adopted by other provinces or by the federal government in national programs. Unless one believes all wisdom lies with Ottawa-based mandarins or Toronto-based charter nationalists, successful new social policies are more likely to be developed if the provinces retain this ability to experiment with social policy approaches.

Second, the growth in public sector debt since the mid-1970s has been caused mainly by "a quite reasonable public demand for a European-style welfare state combined with a quite unreasonable refusal to pay for it." Faced with rising interest payments and a taxpayer revolt, governments have been unable to meet the expectations of those with a stake in continuing public sector growth — notably producer interest groups (for example, public sector unions) and potential users (for example, women's groups lobbying for universal child-care programs). Frustrated by setbacks, these interest groups are now trying to achieve their goals through a social charter and a strong central government.

Third, such efforts will fail. If taxes and deficits are at or beyond their limits, then there is no room for further increases in aggregate government spending. The only way to get more social programs, then, is to improve efficiency. But strong social charters or strong national standards will reduce the accountability of provincial governments, and hence reduce the pressures on these governments to undertake the difficult and politically dangerous process of getting better value for money. Ultimately, a strong social charter and strong national standards are more likely to weaken the welfare state than to strengthen it.

The contributions of Jean-Michel Cousineau and Claude Forget tend to reinforce these arguments. Cousineau focuses on social security expenditures, which currently are more than one-tenth of gross domestic product. There would be a strong case for federal control if the primary objective of these programs were redistributive. More often than not, however, their purpose is to insure against various kinds of risk. Under this interpretation, Cousineau argues, the balance of the argument is in favor of provincial jurisdiction, but with a federal role in the areas of equalization payments and externalities.

Claude Forget brings the perspective of a practical business person with considerable experience in government. While agreeing with many of Richards' recommendations, he questions the relevance of discussions of the division of powers based on "optimality." Rather, significant constitutional change only happens when, as now, there is a widely shared perception of policy failure. This, Forget argues, represents an opportunity as well as a problem, since profound shocks may break bad habits. A major part of the problem is the concentration of bureaucratic power in Ottawa: Canadians are overgoverned. Forget sees a strong link between national standards and the desire of the central bureaucracy to maintain its powers. Similarly, he sees a social charter as reflecting the instincts of a busybody central bureaucracy faced with diminished resources with which to finance social programs. The top priority, according to Forget, should be a substantial reduction in the size of the Ottawa bureaucracy.

John McCallum
Series Editor

Suggestions on Getting the Constitutional Division of Powers Right

John Richards

Of the multiple conundrums that Canadians have created for themselves in this constitutional round, perhaps the hardest to understand — let alone resolve — is the division of powers among levels of government. It is the perennial problem of federal states. Given the country's competing interest groups and discordant nationalist dialogues and given the urgency of arriving at a solution, there are many ways to get this division wrong. This paper presents some ways to get it right.

In outline, I proceed as follows. An opening section sets out some general thoughts on the subject, as well as my own fundamental premises. The next section provides a condensed constitutional history of Canada since Confederation, emphasizing debates over division of powers. The third section introduces some of the theoretical issues relevant to assessing the appropriate division of powers within a federal state. Finally, I offer a simple agenda of nine constitutional recommendations, divided into two categories: the necessary and the highly desirable.

Debating the division of powers is a fundamental aspect of the Canadian identity that probably deserves to be in the Canada clause of the Constitution. In preparing this paper, I have profited from thoughtful criticisms offered by many people. In particular, I thank Allan Blakeney, Rick Harris, Bill Robson, and Bill Watson for investing time in correcting my errors, and in proposing improvements to an earlier draft. I thank Lenore d'Anjou for her rigorous editing of this manuscript. As is traditional in such exercises, all responsibility for the remaining inadequacies is mine, not theirs.

Introduction

In considering the prerequisites for a successful federal state, I agree with the conclusions of the famous Victorian legal scholar Albert Dicey:

> A federal state requires for its formation two conditions.
>
> There must exist, in the first place, a body of countries such as the Cantons of Switzerland, the Colonies of America, or the Provinces of Canada, so closely connected by locality, by history, by race, or the like, as to be capable of bearing, in the eyes of their inhabitants, an impress of common nationality....
>
> A second condition absolutely essential to the founding of a federal system is the existence of a very peculiar state of sentiment among the inhabitants of the countries which it is proposed to unite. They must desire union, and must not desire unity....We may perhaps go a little farther, and say, that a federal government will hardly be formed unless many of the inhabitants of the separate States feel stronger allegiance to their own State than to the federal state represented by the common government.[1]

If we allow that Canada satisfies Dicey's conditions for a federal constitution, it becomes relevant to recall the advice of another constitutional sage, Thomas Jefferson:

> We should thus marshal our government into: (1) the general federal republic for all concerns foreign and federal; (2) that of the state, for what relates to our own citizens exclusively; (3) the county republics, for the duties and concerns of the county; and (4) the ward republics, for the small and yet numerous and interesting concerns of the neighborhood. And in government, as well as in every other business of life, it is by division and subdivision of duties alone that all matters, great and small, can be managed to perfection. And the whole is cemented by giving to every citizen, personally, a part in the administration of the public affairs.[2]

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[1] A.V. Dicey, *Introduction to the Study of the Law of the Constitution*, 8th ed. (1915; reprint, Indianapolis, Ind.: Liberty Fund Inc., 1982), pp. 75–76.

[2] Thomas Jefferson to Samuel Kercheval, July 12, 1816, *Memoirs, Correspondence, and Private Papers of Thomas Jefferson*, ed. Thomas Jefferson Randolph (London, 1829), vol. 4, pp. 296–297.

In other words, the essence of federalism is the division of political sovereignty over the people of a given territory among two or more levels of government. Neither level can have the unilateral ability to change the division. If the central government can unilaterally reallocate jurisdictions, the federation slips into the status of a unitary state (as one can argue has happened to India); if the subnational jurisdictions can collectively adjust the authority accorded to the central government (as is happening in the former Soviet Union), the country becomes a confederation.

Maintaining a true federation requires that its people find practical answers to three classic questions:

- What reasons justify allocation of any particular function to one or another level of government?
- In general, should political matters be decided at the center in the federal capital, or in the provinces, cantons, republics, or states comprising the federation?
- Is it possible to avoid conflicts over the division of powers by either extending justiciable individual rights or using institutions (such as a senate) to give a collective regional voice in the political institutions of the center?

The first question assumes that sovereignty is divisible across functions and that criteria exist to allocate some of them to the center and others to the provinces. The second implies that, in the absence of an overriding reason for allocation to one level or the other, it is possible to choose whichever locus is preferred for political decisionmaking.

Together, these two questions present too many threads too tightly tangled to allow genuinely definitive answers — though the citizens of a federation can find pragmatic solutions and academics can always spin credible tales. One response, implicit in this third question, is to deny the need to come up with answers at all.[3]

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[3] Advocates of justiciation argue that the extension of rights renders superfluous many of the classic problems of division of powers between levels of government. This is the position of some of the more enthusiastic supporters of extension of the Canadian Charter of Rights and Freedoms. Others — including those...

Before proceeding further, let me be explicit about several fundamental premises — some would say biases — that I bring to disentangling the threads of federalism.

1. *Federalism is the optimum form of government when people genuinely have dual loyalties — both to their state/canton/province and to the federation.*

Federalism is desirable when groups of people divided by race, language, large distances, or other meaningful characteristics display strong attachment to their respective local political traditions but nonetheless intermingle geographically and jointly constitute an economic union. It is perfectly reasonable in such circumstances that people want a federal form of government. If the people of a federation redefine themselves in nationalist terms, as did the French after 1789, it is inevitable that a Napoleon will eliminate the *provinces* and substitute for them far less autonomous *départements*.[4]

2. *Although a charter of justiciable rights can be a positive component of a federation and some dimensions of regional interests can be accommodated by political institutions that enable joint central-regional decisionmaking, Jefferson remains correct inasmuch as a well-functioning federation must address the "division and subdivision of duties" between various levels of government.*

It is utopian (though often tempting) to try to avoid the conflicts attendant upon allocating powers between governments. We must inevitably draw two lines in the constitutional sands: one between matters defined as individual justiciable rights and matters subject to legislation enacted by democratically elected parliaments; the

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Note 3 - cont'd.

...inspired by the evolution of the European Community — argue that traditional conflicts over division of powers should be accommodated not by searching for the perfect allocation but by giving a collective representation of regional interests in the political institutions of the center.

[4] The former retained considerable local autonomy under the *ancien régime*, whereas the latter are administrative units entirely subordinate to Paris and exercise symmetric powers determined by reference to national standards imposed at the center.

other between functions best left to the central government and those best left to the lower levels. The lines will shift over time and they will blur when there is need for joint decisionmaking, but lines there must be.

The division of powers within a federation can be compared to the creation of private property rights within a market. Industrial economies cannot approach their productive potential without the accountability and the reward to individual innovation that the institution of private property encourages. Analogously, a reasonably precise division of powers allows politicians to internalize the costs and benefits of policy innovations and management decisions and allows citizens to hold their politicians accountable for the results.

3. *The constant threat to federal states is irreconcilable nationalisms among groups within the federation; these differences often rise from or are heightened by shocks in the environment.*

René Lévesque often used the image of the Canadian federation as a bottle housing two warring scorpions. He was surely wrong to imply that life as a solitary scorpion in one of two bottles would be a better fate. Relative to the history of other federations in which conflicting nationalisms do not respect limits and people do indeed behave like warring scorpions — consider the Serbs and Croats in Yugoslavia, and the Sikh and Tamil separatists in India — the history of Canadian federalism has been far more positive than Lévesque's image implies.

He was right, however, to emphasize the destructive potential of conflicting nationalisms, even the domesticated variants in Canada. The essence of nationalism is to substitute a uniform national identity for cultural, regional, and other diversity, to insist on complete sovereignty for the "nation" however defined, and to blame other nations for domestic problems. Nationalism is a natural enemy of federalism.

Since the 1960s, a succession of shocks within Canada has generated four potentially destructive nationalisms: a demand for independence among the Québécois;[5] an elevation of aboriginal political frustrations into a nationalist agenda for self-government; a left-wing "charter nationalism"; and a right-wing populist nationalism. Despite exacerbated political frustrations, however, most Canadians still possess enough of Lord Dicey's dual loyalty to make federalism the optimum form of government.

A simple piece of evidence is the response to the 1990 poll question: "Do you feel you are more a citizen of Canada or more a citizen of this province?" Forty-nine percent of respondents identified more with Canada than with their province. By region, the percentage identifying as Canadians first was highest in Ontario and lowest in Quebec. But even 38 percent of Ontario residents identified primarily with their province and 33 percent of Quebec residents identified primarily with Canada.[6] Of course, this poll did not assess the intensity of commitments or the willingness to trade off one loyalty for another, so it does not prove the presence of Dicey's dual loyalty; nonetheless, it shows a geographic intermingling of people with different rankings of loyalties.

4. *It is intellectually dishonest to compare functioning federal states to a utopia without political conflict. Much of the conflict within federations is healthy, like competition among firms in competitive markets.*

Critics diverge sharply on the desirable constitutional alternative to federalism, yet they often agree in describing it as a kind of purgatory: an unsatisfactory halfway house toward a more "advanced" form of government, such as a unitary state, or dissolution into two or more separate sovereign states. Pierre Trudeau and Jacques Parizeau are obvious Canadian examples of this tendency.

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[5] I use "Québécois" throughout to refer to those Quebec citizens whose maternal language is French. The use of this shorthand does not imply that those Quebec citizens whose maternal language is other than French are any less legitimate citizens of the province.

[6] M. Adams and M.J. Lennon, "The Public's View of the Canadian Federation," in R.L. Watts and D.M.Brown, eds., *Canada: The State of the Federation 1990* (Kingston, Ont.: Institute of Intergovernmental Relations, Queen's University, 1990).

Heaven for the former is a Canada in which the "boyars" are humbled and the citizens united by respect for the individual rights embodied in the Charter of Rights and Freedoms. The latter paints an equally bright alternative of two unilingual sovereign countries, both endowed with strong, efficient central governments that co-manage, without fuss, the shared economic union. Although the state of grace for the one is hell for the other, they agree in condemning the federal exercise of dividing jurisdictions.

In contrast to both, I believe decentralization of functions within a federation often serves as a political analogue to competitive markets. In Canada, this arrangement has allowed particular provinces to innovate independently of the rest and played a crucial role in the postwar growth of a good — if far from perfect — welfare state.

5. *If, as Montesquieu states, democracy is the most demanding form of government in terms of the responsibility placed on citizens and politicians, then federalism is the most demanding form of democracy. Relative to unitary states, federations require more formal institutional checks and balances to monitor the federation and maintain the constitutional equilibrium.*

Since the division of powers in a federation can never be as watertight as that between sovereign states, an interest group constrained by one level of government may seek to realize its goals by changing the allocation of jurisdictions. If interest groups regularly engage in such jurisdictional lobbying and if politicians seek popular support by obliging them, the gains from a stable constitutional order are lost. It becomes impossible for any government to internalize the costs and benefits of its policy decisions and to be held accountable for the results.

The two obvious checks on the conduct of politicians in a federal state are the courts and a second chamber. Given Canadians' massive mistrust of their governments, both institutional checks need to operate effectively. At present only the courts do so; the Senate remains a home for patronage political appointees and lacks legitimacy. The result is that Canadians at present are too quick to rely on litigation and judge-made law.

A Little History

Canada in 1867: A Quasi-Federation

John A. Macdonald and his closest allies, such as Charles Tupper, were genuine Canadian nationalists and simultaneously "typical mid-Victorian colonial politicians...[who] assumed that they were legitimate heirs of the British constitutional heritage and full participants in the British political experience."[7] They wanted to forge a unity among colonists in British North America analogous to that prevailing among Englishmen. It would be unfair to reduce their nationalism to economic concerns alone, but absolutely central to their political vision was that Confederation be a means of expanding the common market available to colonial businessmen. In particular, it was to be a way to accelerate railway construction by expanding the aggregate government ability to guarantee the debt incurred.

Macdonald and his allies profoundly distrusted federalism. They wanted a unitary state based on the British precedent of parliamentary sovereignty.[8] Federalism with its legitimation of "states' rights" had, they concluded, led to the disastrous civil war raging on their southern border. But Macdonald was also a pragmatist. Although his primary goal was certainly not accommodation of Quebec's linguistic, religious, and cultural concerns or of the regional loyalties of the Maritime colonies, he did not ignore the previous century of political experience in British North America.

The *Quebec Act* of 1774 had inaugurated a primitive form of federalism that accorded the conquered subjects of New France collective political rights over language, religion, and education. It had been quite successful in bringing about a limited loyalty to the British Crown, especially at the time of the American revolution. The Québécois perceived the alternative as an alien product of the Enlightenment — individual liberty leading to cultural suicide. Macdonald recognized that political initiatives for assimilation, the most dramatic being the 1840 *Act of Union* inspired by Lord Durham's report, had all failed.[9]

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[7] D. Creighton, *Canada's First Century* (Toronto: Macmillan, 1970), p. 9.

[8] Ibid., chap. 1.

Thus, Macdonald's negotiations with George-Étienne Cartier became what Frank Scott has characterized as an analogue of the relationship between Alexander Hamilton and Thomas Jefferson.[10] Macdonald was well aware of *The Federalist Papers*, and an admirer of Hamilton's arguments therein. Although Cartier did not share Jefferson's eighteenth-century Enlightenment view of individual rights, he agreed that regional, territorially based groups were legitimate bases on which to found a federation. Cartier secured support for Confederation within Quebec on the basis of the autonomy it would afford the Quebec assembly over education, religious, and cultural matters. Debate within Quebec turned on the question of which constitutional arrangement would afford more autonomy: the status quo, in which the British Parliament acted as ultimate guarantor, or an untried federation? A majority, by no means overwhelming, of the Québécois elite opted for the latter.

Nor could Macdonald minimize the strength of regional loyalties. The first threat to post-Confederation Canada did not pit English against French. In 1868, Joseph Howe's Liberals won the Nova Scotia government with a mandate to pull the province out.[11]

The net result of constitutional negotiations was the *British North America Act*. It is a federal constitution but one in which the center has a number of overriding powers that give it the upper hand: disallowance of provincial legislation; allocation of residual powers to the center; central control of appointments to the Senate and the Supreme Court; plenary taxation powers at the center with only restricted ones in the provinces; complete control of trade and commerce; appointment of lieutenant governors, who have the power to reserve Royal Assent to provincial legislation; and a declaratory power allowing Ottawa to assume jurisdiction over "local works and undertakings." The *BNA Act* has been described, quite reasonably, as a mandate for a quasi-federation.

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[9] The *Act of Union* created a state that was unitary in form, but it could not function as such. After several years, the province of Canada operated *de facto* as a confederation, requiring double majorities of anglophone and francophone representatives in order to implement major decisions.

[10] Frank Scott, "French Canada and Canadian Federalism," in A.R.M. Lower et al., eds., *Evolving Canadian Federalism* (Durham, N.C.: Duke University Press, 1958).

[11] Howe feared, quite rightly as history has shown, the impact on the Maritime colonies of finding themselves behind tariff walls erected to promote industrialization in Central Canada. Macdonald solved the immediate crisis by using his mastery of the art of patronage to co-opt Howe into the federal cabinet.

Canada in 1927: Federal Equilibrium

What had transpired by Canada's diamond jubilee in 1927?

Successive governments in Ottawa had realized the ambition embodied in Macdonald's National Policy.[12] Canada had been transformed from North America's Yugoslavia — loosely joined remnants of disbanded empires — into a functioning country of continental dimensions. Ottawa had subsidized not one but three transcontinental railways, filled the Prairies with settlers flying the Red Ensign rather than the Stars and Stripes, and induced a good deal of tariff-protected industrialization.

By 1927, other political initiatives, primarily local and provincial, had begun to blunt the extremes of income distribution and provide basic public goods. Provincial governments supplied education services and welfare for the indigent as well as some simple social insurance programs — such as workers' compensation and crop insurance against hail. Total government expenditures grew substantially in the 1920s, but by 1927 they still constituted just

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[12] The National Policy was a success by the rhetoric of leading contemporary politicians, but in the name of nationbuilding it probably lowered productivity relative to the outcome of a competitive market process. Federal railway subsidies, for example, induced premature and inordinately excessive investment in transportation infrastructure. Nationalist concerns forced recourse to all-Canadian routes north of the Great Lakes, rather than routes through the United States that would have permitted far more short-haul traffic and hence lower average fixed costs per ton-mile. The tariff distorted least-cost locational decisions for industry. Attempting to measure these inefficiencies is a minor academic industry among economic historians.

16 percent of GDP — roughly a third of the present ratio. Of these expenditures, more than two-thirds were made by provincial and local governments. Ottawa's transfers to the provinces amounted that year to an insignificant 0.3 percent of GDP.[13]

The precedents for Canada's future welfare state were probably most evident on the Prairies, where farm-based reform movements had broken with the old-line national parties and won several provincial elections. In general, these governments provided efficient administration plus social services that were novel and generous by contemporary standards. And numerous local governments on the Prairies were operating municipal health insurance schemes, forerunners of the province-wide programs Saskatchewan would introduce after World War II.

The Shape of Contemporary Federalism

In 1927, the Judicial Committee of the Privy Council still served as Canada's final court of appeal on constitutional matters. In a series of decisions delivered over the previous 60 years, their lordships had recognized far more fully and explicitly the underlying dual loyalties of Canadians than had the authors of the *British North America Act*. A typical example of the Judicial Committee's handiwork was Lord Watson's 1892 decision. Ottawa had challenged New Brunswick's power to claim priority over other creditors in a business bankruptcy. In dismissing the federal argument, Lord Watson unequivocally asserted that a provincial government

> derives no authority from the Government of Canada, and its status is in no way analogous to that of a municipal institution, which is an authority constituted for purposes of local administration. It possesses power, not of administration merely, but of legislation, in the strictest sense of that word; and, within the

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[13] Canada, Dominion Bureau of Statistics, *National Accounts Income and Expenditure 1926–1956* (Ottawa: Dominion Bureau of Statistics, 1962), pp. 76–77.

> limits assigned by section 92 of the [British North America] Act of 1867, these powers are exclusive and supreme.[14]

Such an interpretation was consistent with that of Quebec and of some Maritime Fathers of Confederation; it was certainly not consistent with Macdonald's.

The Judicial Committee's decisions did not contain many statements of first principles, but one can infer a theory of federalism that is worth summarizing because of its continuing relevance.

1. Powers enjoyed by a level of government should generally be exclusive to that level. "While the ship of state now sails on larger ventures and into foreign waters she still retains the watertight compartments which are an essential part of her original structure," wrote Lord Atkin in 1937.[15]

2. Language rights are basically subject to the will of the majority within a local territory. The British constitutional tradition assumes individual rights are adequately protected by the conventions of parliamentary government and the precedents of the common law. Consequently, the *BNA Act* and subsequent imperial statutes creating additional provinces contained no bill of individual rights. A few provisions did, however, address collective minority rights: for example, section 93 of the *BNA Act* provided for denominational schools, and section 133 imposed bilingual requirements on the Dominion Parliament and the Quebec assembly.

Canada's most contentious minority language issue was use of French in schools and in the governments of provinces other than Quebec. In the few cases in which the Judicial Committee dealt with the matter, it upheld majority sentiment embodied in statute or government regulation over assertions of minority rights. Members of the committee extrapolated the pragmatic conclusion drawn from two centuries of British colonial rule: central power should be limited to those functions essential for the conduct of commerce and maintenance of Pax Britannica; the local colonial population should exercise jurisdiction over language. ("In the British Empire there are people of many languages. The use of these does not affect the loyalty of the people to the Crown," noted Lord Buckmaster in a 1917 decision.)[16] The effect was the right of each province — Quebec as well as the others — to regulate the use of language in its own jurisdiction.

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[14] *Liquidators of the Maritime Bank of Canada v. Receiver General of New Brunswick*, 1892, cited in P.H. Russell, ed., *Leading Constitutional Decisions*, 3rd ed. (Ottawa: Carleton University Press, 1982), p. 53.

[15] *Attorney General of Canada v. Attorney General of Ontario*, 1937, cited in Russell, ed., *Leading Constitutional Decisions*, p. 130.

3. Local matters should be regulated by provincial governments. Section 92(16) of the *BNA Act* stated explicitly that "all matters of a merely local or private nature in the province" were to be under exclusive provincial jurisdiction. This was the last of the provincial powers enumerated in section 92, and the use of the word "merely" suggests the authors of the act considered it a throwaway. The Judicial Committee, however, took the idea seriously. They assumed many more matters to be local than a casual reading of the *BNA Act* would suggest. As a corollary, they restricted the application of federal authority under the "peace, order and good government" clause to matters that were transparently national in scope or responses to an emergency such as war.

4. The federal government and the provinces have joint responsibility for economic regulation. The Judicial Committee assumed without question the value of private property, the desirability of a well-functioning common market throughout Canada, and the idea that government regulation of market activity should not be intrusive. To the limited extent government was expected to regulate economic activity, both levels were able to do so. Ottawa could regulate under many heads; the Judicial Committee interpreted

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[16] *Ottawa Roman Catholic Separate School v. Mackell*, 1917, cited in Russell, ed., *Leading Constitutional Decisions*, p. 458.

section 92(13) ("property and civil rights in the province") to permit broad provincial regulation of intraprovincial economic matters.

The Federal "Spending Power"

Nineteen twenty-seven was an important date in the evolution of the Canadian welfare state — and in the unraveling of the Judicial Committee's classic federal model for Canada. In that year, William Lyon Mackenzie King introduced a national old age pension scheme to be cost-shared with the provinces. In other words, Ottawa made conditional grants in an area that was then unambiguously one of exclusive provincial jurisdiction.[17]

It was a prime example of use of the federal spending power — expenditure by the federal cabinet of general revenues on a purpose it deems appropriate, whether or not it is within federal jurisdiction — and it came about quite pragmatically. In the 1925 election, King's Liberals had elected only a minority of MPs. He needed third-party support to remain in power. J.S. Woodsworth, MP from Winnipeg North Centre and head of the small Ginger Group of left-wing Progressives, agreed to provide the support in exchange for King's commitment to a pension program. Some provincial politicians objected, most forcefully in Quebec, to federal spending on pensions as an intrusion into provincial jurisdiction. But ultimately no politician, even in Quebec, was prepared to see constituents taxed to support benefits they did not receive. All the provinces signed federal-provincial pension agreements.

Now a basic, universal, state-financed old age pension introduces a degree of income redistribution that most citizens approve. (Evidence of this approval is to be found in the fact that every advanced industrial country has adopted such programs.) Probably, this exercise of the federal spending power simply accelerated what provinces would have undertaken on their own initiative at a later date. However, the plenary taxing power of Ottawa plus the ability to alter unilaterally the relative cost of provincial options is not consistent with the federal concept of divided jurisdiction.

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[17] Only by a 1951 amendment to the *BNA Act* did pensions became a concurrent jurisdiction.

Summary

In summary, Canada had achieved considerable success with its federal experiment by 1927. Primarily because of federal initiatives, it had a continental industrial economy; primarily because of provincial initiatives, it was developing a modern welfare state. Over the previous 60 years, numerous distributional issues had pitted the regions against each other and against Ottawa. Religious and linguistic conflicts had also arisen. But at the time, the Canadian federation had achieved an equilibrium.

Canada, 1927–67: Plus ça change plus c'est la même chose

The diamond jubilee of Confederation in 1927 took place at a moment of relative prosperity and constitutional equilibrium. Likewise, the centenary celebrations in 1967 found Canadians in a relaxed state of self-confidence: Ottawa and the provinces were jointly undertaking major expansion of the Canadian welfare state, and a renaissance in Quebec had transformed the traditional defensive nationalism of the Québécois into a lively set of new options. But shortly after both celebrations, we lost our constitutional equilibrium.

The first few years after 1927 went well enough. With little controversy, Canadians undertook some constitutional housekeeping. Ottawa acquired unambiguous control of foreign policy with enactment of the Statute of Westminster, and the Western provinces acquired a status equivalent to the others by obtaining title to Crown lands within their respective borders.

The period's first shock to constitutional equilibrium was the Great Depression. Its impact on per capita incomes varied dramatically across the country, affecting most severely those provinces —

the Prairies and Maritimes — whose economies depended disproportionately on export markets. Increased tariff protection by Ottawa exacerbated the problem by raising the cost of factor inputs to export sectors of the economy.

The major government report documenting the contemporary intellectual response was that of the Rowell-Sirois Commission.[18] The Depression had reduced some provinces to virtual bankruptcy and, outside Quebec, conventional wisdom in Canada assumed that political solutions entailed centralization. As in the United States, many Canadians were impatient with the checks and balances of federalism. The Rowell-Sirois Commission recommended, for example, federal assumption of responsibility for a national unemployment insurance program; the transfer to Ottawa of the right to impose income tax — an increasingly important source of revenue; and a form of equalization grants funded by Ottawa to permit poorer provinces to maintain services without recourse to exceptionally high taxation.

The provinces formally rejected much of the Rowell-Sirois report, but a great deal of centralization occurred anyway because of a second shock: World War II. It dramatically increased the importance of the defense function, an unambiguously federal responsibility. In 1944, the peak year of defense expenditures, Ottawa was responsible for five-sixths of government spending, a complete reversal of relative federal and provincial shares of spending in 1927.

The Division of Powers and the Growth of the Welfare State

Lord Durham and de Tocqueville made their respective observations on Canada and the United States during the 1830s. Had they returned from the grave a century later to observe once again the state of North American democracy, they would probably have concluded the United States was more likely than Canada to generate a European-style welfare state. They would have noted that although the 1787 U.S. constitution had implied a more decentralized federation than had the *British North America Act*, the U.S. Supreme Court had since given legal sanction to more centralization than had the Judicial Committee for Canada. Relying on the conventional wisdom of the 1930s, they would have assumed that provincial, state, and local governments were inevitably dominated by conservative local elites and only central governments were capable of harnessing the general will to realize significant new social policies and redistribute income. The obvious conclusion: more public sector entrepreneurship would occur in the United States than in Canada. Supporting evidence was all around. The ratio of union to nonunion workers was higher in the United States than in Canada; the liberal New Deal in the United States had created more generous social security programs in many domains than existed in Canada. Yet the conclusion would obviously have been wrong. After World War II, it was Canada, not the United States, that developed a European-style welfare state to blunt the harsh edges of capitalism.

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[18] Canada, Royal Commission on Dominion-Provincial Relations, *Report* (1940; reprint, D.V. Smiley, ed., Toronto: McClelland & Stewart, 1963). Hereinafter, "the Rowell-Sirois report."

Why? Some explain this postwar development in terms of Canadians' having a more collectivist political culture than do Americans. The difficulty with this explanation is twofold. First, comparative empirical surveys of opinion find that Canadians and Americans hold remarkably similar attitudes on many dimensions of public policy. Second, if Canadians' collectivist political culture is the explanation, why did Americans innovate more extensively in social policy during the 1930s?

What I find a more persuasive explanation is that, as citizens of all Western industrial societies made increasing demands on their respective governments for welfare state programs, Canada enjoyed — by the historical good luck of the Judicial Committee's reinterpretation of the *BNA Act* — a more efficient constitutional division of powers than did the United States. The provinces retained overall responsibility for social policy, and Ottawa enjoyed plenary taxing powers, permitting it to undertake a reasonable level of interprovincial redistribution. The result was that during the quarter century following World War II, Canada restored its constitutional equilibrium as the provinces and Ottawa jointly created a reasonably good welfare state.

Provincial jurisdiction over social policy is more efficient than centralized power in two senses. First, in the static sense, the administration of many public social programs probably offers some important diseconomies of scale. Although variance is undeniably high across provinces and over time, provincial administration in this domain is probably, on average, more efficient than federal. The Atlantic provinces may be too small for efficiency, but the administrative experience of the two smaller Prairie provinces indicates that a population of approximately a million is large enough to realize efficient delivery of social programs. And as discussed later, larger political units face more acute problems of inefficient interest-group bargaining.

Second and more important, provincial jurisdiction is more efficient in the dynamic sense in that it allows entrepreneurially innovative governments to tax and spend on major experiments in social policy independent of the political preferences elsewhere in the country. The most important example of such provincial entrepreneurship was Saskatchewan's introduction of universal hospital insurance in 1947 and universal medical insurance in 1962. Allan Blakeney, one of the key provincial entrepreneurs responsible for the shape of the Canadian welfare state, has stated:

> There is no fundamental reason for Canadians to be further to the left politically than Americans, yet we Canadians have undeniably undertaken more significant political experiments than the Americans. Why? The key to an explanation is that Canadian federalism has preserved enough powers at the provincial level for provinces to serve as social laboratories, whereas American federalism has so reduced states' rights that significant political experiments can only emanate from Washington....To launch a major experiment in social policy via the national government requires a majority of a parliament representing the whole country. That is far less likely to occur than

> that a majority of a state or provincial legislature opt for the experiment. When you talk to an American about medicare, he assumes it must be a federal program and then proceeds to talk about the problems: the inefficiencies of too large a bureaucracy in Washington, the resulting excessive costs, etc. Had a Farmer-Labor government in Minnesota had the power to introduce a statewide medical care insurance program, then, after a decade or so, I suspect citizens elsewhere in the U.S. would have insisted on a national equivalent.[19]

Once provincial experiments demonstrated the net benefits to be derived from social programs such as universal health insurance, overwhelming popular support existed to extend them across the country. Ottawa, in turn, induced compliance in the socially conservative provinces by resorting to two instruments: equalization payments to "have-not" provinces, and exercise of the spending power to introduce conditional grants that, as in the earlier case of old age pensions, presented provincial governments with offers they could not refuse.

Also important in explaining the growth of Canada's welfare state was the work of entrepreneurial provincial parties. The example of Saskatchewan under the New Democratic Party (NDP) and its predecessor the Co-operative Commonwealth Federation (CCF) was crucial. Other significant examples came from the governments of Quebec, both Liberal and Parti Québécois, after 1960. Both old-line parties played an important role at the federal level. John Diefenbaker's Conservative government made hospital insurance a national shared-cost program and appointed the Royal Commission, chaired by Justice Emmett Hall, that proposed national adoption of the Saskatchewan model of health insurance. Justice Hall's recommendations were then implemented by Lester Pearson's Liberal administration during the second half of the 1960s.

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[19] A. Blakeney, "Decentralization: A Qualified Defence," in J. Richards and D. Kerr, eds., *Canada, What's Left?* (Edmonton: Newest Press, 1986), p. 148. Blakeney occupied senior portfolios in the Saskatchewan cabinet — including that of health — at the time universal medical care insurance was introduced in the early 1960s; he was later premier of the province.

Canada 1967 — ?: The Scourge of Conflicting Nationalisms

Why has Canada lost the equilibrium it had slowly reestablished by the 1960s? Briefly, it has suffered four shocks with important constitutional ramifications, and to each our political leaders have responded inadequately, allowing constitutional stresses to accumulate. The equilibrium would probably have survived any one of the shocks singly, but it has been lost under their combined effect.[20]

Cultural and Economic Stress among Aboriginal Canadians

One shock has been the profound and continuing crisis of aboriginal Canadians. Over the past two generations, the proportion living off-reserve and in cities has increased significantly. This change has been positive inasmuch as urban, off-reserve aboriginals average higher incomes and are better educated than their rural, on-reserve kin.[21] But the migration has also intensified interaction between white and aboriginal societies, which in turn has exacerbated the syndrome of native cultural anomie, leading to increased family disintegration and unemployment among all aboriginal Canadians, regardless of location.

Had public policy responses been more innovative and effective, aboriginal political demands might never have assumed a constitutional dimension, but that line of thought is now hypothetical speculation. Native politics have become a form of nationalism.

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[20] This section revises and expands arguments made in an earlier contribution to the Canada Round series. John Richards, "A Social Charter: Two Cheers but Not Three," in Havi Echenberg et al., *A Social Charter for Canada? Perspectives on the Constitutional Entrenchment of Social Rights*, The Canada Round 9 (Toronto: C.D. Howe Institute, 1992), pp. 66–71.

[21] For surveys of relevant data, see, for example, A.J. Siggner, "The Sociodemographic Conditions of Registered Indians," *Canadian Social Trends*, Statistics Canada, Cat. no. 11-008, Winter 1986; and Canada, Department of Indian and Northern Affairs, *Basic Departmental Data*, annual.

The small but articulate native leadership across the country argues that aboriginals constitute a "distinct society" as much as, if not more than, does Quebec. They are demanding that native-controlled governments become a third level within the federation, governments with a constitutional standing as solid as that of Ottawa and the provinces. Despite these leaders' lack of consensus in defining self-government, an overwhelming majority of aboriginal Canadians support them in demanding a large measure of political autonomy from white administration.

The Quiet Revolution in Quebec

Perhaps the most profound constitutional shock has been the *révolution tranquille*. Central to this complex social renewal was the insistence of the Québécois that the provincial government legislate to promote French as the dominant language of instruction and work within Quebec. A succession of provincial language laws — the Parti Québécois's Bill 101, the Charter of the French Language, is the most important — has achieved that goal. The *revers de la médaille* has been restriction in the use of English. Access to English-language instruction is restricted, major firms are obliged to operate in French, and most signs in languages other than French are forbidden.

The heart of the language problem has always been Montreal, which contains one-third of the province's population. Francophones are not a secure majority there. The world's second-largest francophone city has experienced volatile shifts in the relative strength of its several linguistic communities. For example, between 1941 and 1986, the anglophone community declined from 26 to 20 percent of the population, while the allophone community increased from 10 to 18 percent. Coincidentally, the two shifts offset one another, and the francophone share remained nearly constant at 63 percent.[22]

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[22] M.M. Termote, "L'Évolution démolinguistique du Québec et du Canada," in Quebec, Commission sur l'avenir politique et politique constitutionnel du Québec [Bélanger-Campeau Commission], *Éléments d'analyse institutionnelle, juridique et démolinguistique pertinents à la révision du statut politique et constitutionnel du Québec* [Background papers], vol. 2 (Quebec, 1991).

Underlying Quebec's language laws is the theory that the linguistic choices made by many people, particularly allophone immigrants, are based on a calculation of the net benefit of learning the country's "major" language (English) relative to its "minor" language (French). The benefits of speaking a language depend critically on the number of people speaking it. Since the cost of learning either English or French is similar, the net benefit of English will inevitably outweigh French in a free linguistic market. This choice has an external effect, however; it lowers the value of the francophone majority's linguistic investment in their "minor" language.

The theory of language as an investment with external effects implies that ultimately there is no way to avoid the painful policy question: Which language should predominate in communities, such as Montreal, in which two linguistic communities interact extensively? Language legislation can probably preserve French — at the expense of English. Treating the English-French choice as an individual civil liberty will probably mean the transformation of Montreal into a majority anglophone city. On the basis of the implicit social contract of the *BNA Act* and the utilitarian argument that francophones constitute a majority within Quebec, the Quebec government has opted to promote French — subject to significant minority language rights for anglophones.

The federal Liberal government of Pierre Elliott Trudeau recognized the disadvantage of French relative to English more explicitly than any previous Canadian government. Ottawa vigorously pursued bilingualism within the federal jurisdiction and provided generous subsidies to official language minorities. The principle underlying federal policy was, however, that the decision to use either of the two official languages should be an individual civil liberty. The potential for conflict with Quebec City was obvious.

In response to election of the Parti Québécois government in 1976, Ottawa established the Task Force on Canadian Unity (the Pepin-Robarts Task Force). It recommended in 1979 that "each provincial legislature...have the right to determine an official language or official languages for that province, within its sphere of jurisdiction."[23] The following year the Quebec Liberal Party, under the leadership of Claude Ryan, produced a second comprehensive constitutional review — usually called the Beige Paper for the colour of its cover — that arrived at similar conclusions.[24] It described Quebec as a "distinct society" and proposed that the provinces enjoy the right to legislate over language, subject to minority language rights and a bilingual federal government.

Trudeau, with his long-standing ideological opposition to Québécois nationalism, rejected both reports, but for tactical reasons he was less than explicit in doing so before the 1980 Quebec referendum on sovereignty-association. In campaigning beside Claude Ryan for the *non* side, he made an ambiguous promise of "renewed federalism." He subsequently interpreted the *non* majority as a mandate to advance his own constitutional theses, becoming quite explicit in rejecting the Pepin-Robarts report, the Beige Paper, and everyone who sought to grant Quebec special status over language. The result was the 1982 package containing a new constitutional amending formula, various amendments to the *British North America Act*, and, most important, the Charter of Rights and Freedoms.

The Charter explicitly confirmed the desire of Trudeau and most of the "Rest of Canada" (ROC) to treat language as an extension of justiciable civil rights and to ignore the economics of linguistic choice. It referred to English and French as the "official languages of Canada" (section 16(1)) but mentioned no special role for Quebec in promoting French within its borders. Some clauses of the Charter explicitly overrode provisions of Bill 101; other clauses were sufficiently ambiguous that the Supreme Court might be able further to erode Quebec linguistic jurisdiction. And in 1988, the court did just that, ruling Bill 101's unilingual commercial sign provisions contrary to the Quebec and federal charters.[25]

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[23] Canada, Task Force on Canadian Unity, *A Future Together*, chaired by Jean-Luc Pepin and John Robarts (Ottawa: Supply and Services Canada, 1979), p. 121.

[24] Quebec Liberal Party, Constitutional Committee, *A New Canadian Federation* (Quebec, 1980).

[25] *Ford v. Attorney General Quebec*, 1988. See M. Mandel, *The Charter of Rights and the Legalization of Politics in Canada* (Toronto: Wall and Thompson, 1989).

The 1982 constitutional package was endorsed by Parliament and nine of the ten provincial legislatures. That it had the legitimacy of support from the Liberal members of Parliament from Quebec — 74 of the total Quebec caucus of 75 — reflected more the strength of party discipline in Canadian politics than the nature of Quebec society. In the Quebec National Assembly, a resolution rejecting the package was supported by a majority of the opposition Liberal MNAs as well as by the PQ government.

The federal Conservative government of Brian Mulroney and the provincial Liberal government of Robert Bourassa were subsequently elected in part to undo this constitutional polarization. In drafting the Meech Lake Accord, they sought to resurrect the "distinct society" concept from the Beige Paper, allowing the government of Quebec "to preserve and promote the distinct identity of Quebec."

The PQ's adoption of Bill 101 had the unintended consequence of undercutting demand for Quebec political sovereignty — why separate if linguistic concerns could be satisfied within the federation? The Supreme Court's commercial sign decision had the unintended consequence of undercutting both the political viability of language policy as a matter of justiciable civil liberty and the acceptability of the Meech Lake Accord. Most journalistic and academic commentators writing before the Supreme Court decision had thought Quebec nationalism in retreat after loss of the 1980 referendum.[26] But it immediately and vociferously asserted itself to defend Quebec's language laws. In response, the Quebec government enacted Bill 178, using the "notwithstanding" clause of the Charter (section 33) to override the Supreme Court's decision. In turn, public sentiment in ROC became equally vociferous in criticizing Quebec's language policy and turned against the Meech Lake Accord. Although the federal Parliament and many provinces had already ratified the accord, it now proved impossible to secure the required unanimous approval of the provinces.

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[26] See, for example, D.V. Smiley, *The Federal Condition in Canada* (Toronto: McGraw-Hill Ryerson, 1987).

Large Commodity Price Movements

The third shock has been the large, unexpected movements in the international prices of commodities, particularly oil, over the past two decades. These price changes have generated dramatic redistribution of regional income — and demands from the losers for offsetting public policy.

Optimal federal policy would have required simultaneous respect for the efficiency advantages of provincial resource management, exercise of the federal taxing power to redistribute a good deal of windfall rents out of the resource-rich provinces, and reliance on high domestic prices to realize conservation goals. Instead, successive federal governments placed excessive emphasis on the goal of interregional redistribution. The culmination was the National Energy Program (NEP), introduced in 1980, which imposed low domestic prices and made available large subsidies to Canadian-owned firms willing to develop inefficient, high-cost reserves located outside provincial boundaries. The regional hostility to this program was the catalyst for a new wave of right-wing populist nationalism in Western Canada.

The rational core of this populist nationalism is mistrust of the federal government's pursuit of inefficient policies designed to redistribute income toward marginal voters in the more populous provinces of Central Canada at the expense of productive regional economies in Western Canada. Ottawa's cardinal sins, according to the rhetoric of this nationalist constituency, were the NEP and the awarding — by a Quebec-based prime minister — of the CF-18 aircraft repair contract to a Montreal-based firm over a Winnipeg-based competitor, even though the Department of National Defence had clearly stated the technical superiority of the latter. The response has been adamant insistence on a Triple-E Senate (elected, equal, and effective) that would allow the peripheral provinces to exercise an effective veto over such policies.

Public Sector Debt and Charter Nationalism

The fourth shock has been the growth in public sector debt, the result of Canadians' quite reasonable demand for a European-style welfare state combined with a quite unreasonable refusal to pay for it (see the box and accompanying table on pp. 28–29 for a summary of public sector spending).

The last year in which the total public sector — Ottawa plus provinces, local governments, and hospitals — was in surplus was 1974. Deficit financing was justified during the two major recessions of the past 15 years, but our politicians' inability to achieve fiscal balance over the business cycle has generated predictable negative macroeconomic consequences, such as increasing both real interest rates and the dollar exchange rate required to maintain domestic price stability.

Under the best of circumstances — with each level of government unambiguously accountable for specific components of public spending — politicians would have found it tough to generate public support sufficient to balance their respective budgets. Canadians value their social programs highly, but the cost is obviously close to the ill-defined limit on aggregate willingness to pay. The controversy surrounding introduction of the goods and services tax (GST) is just the most dramatic example of the existence of such a limit and of public opposition to any further increase in the share of GDP absorbed by taxes. The fact that debt servicing has absorbed an ever-higher share of public spending has obviously exacerbated the problem of balancing the budget while maintaining the quality of social programs.

On the one hand is a nascent tax revolt. On the other is a loose coalition of interest groups with strong expectations of continued public sector growth. Tom Courchene has coined the phrase "charter nationalism"[27] to describe the perspective of this coalition, which includes producer groups, such as public sector unions, and groups desirous of expanded public services, such as lobbyists for universal child care. The tactical goal of members of the coalition is to expand the role of the Charter of Rights and Freedoms in determining public policy. Their perspective is a form of nationalism inasmuch as they have defined the *raison d'être* of the country in terms of social policy. Typically, they want the existing Charter amended to create explicit justiciable rights to "adequate" levels of a broad range of social services, thereby shifting the locus for determining social policy from governments to the courts. This coalition has been influential within the Liberals and, *a fortiori*, within the NDP. (Indeed, a social charter has been the principal constitutional demand of the Ontario NDP.)

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[27] T.J. Courchene, *Forever Amber*, Reflections 6 (Kingston, Ont.: Institute of Intergovernmental Relations, Queen's University, 1990); and idem, *The Community of the Canadas*, Reflections 8 (Kingston, Ont.: Institute of Intergovernmental Relations, Queen's University, 1991).

Given the worsening fiscal crisis, governments have been repeatedly obliged to frustrate the expectations of the charter nationalists. Here are some of the battles since 1974:

- The imposition of wage and price controls in 1975 had among its goals the reduction of public sector wage increases. It met with vehement union opposition.
- In 1977, Ottawa transformed most conditional grants to the provinces into block grants and tax points under Established Programs Financing (EPF), thereby eliminating the temptation for provincial politicians to spend "50-cent dollars." The reform was actively opposed by interest groups whose funding was potentially affected.
- Relative to European countries in the Organisation for Economic Co-operation and Development, Canada devotes a high proportion of GDP to outright transfers to the unemployed and a low proportion to "active" labor market policies intended to retrain and relocate workers. Yet many groups have lobbied vociferously in Ottawa and in provincial capitals, particularly in Atlantic Canada, on behalf of the status quo and against changes in Canada's unemployment insurance program. Most of these groups represent those with fixed physical assets or human skills that would be devalued under policies that encouraged labor mobility.

Public Sector Spending, 1961–89

Table 1 summarizes the five salient characteristics of public sector spending (measured as a share of GDP) during the past three decades:

1. Expansion of social spending derived primarily from provincial governments (municipal governments and hospitals are included in this category). They increased their spending by approximately 7 percentage points from the early 1960s to the mid-1970s. Since then, provincial spending has been constant except for a rise during the serious 1981–82 recession and its aftermath.

2. Federal program spending net of transfers to the provinces, even including deficit spending during the 1980s recession, has remained remarkably constant — within a band of 3 percentage points. The Mulroney government has reduced program spending from the levels induced by that recession, but in 1989 it was still within 1 percentage point of the Trudeau government's level in 1981 and of the average in the late Diefenbaker years.

3. Federal transfers to the provinces — the three principal components are equalization payments, Established Programs Financing, and payments under the Canada Assistance Plan — grew by nearly 2 percentage points between the early 1960s and the mid-1970s. They have remained relatively constant since, although they are projected to decline as part of the federal deficit-control program.

4. Federal and provincial own-source revenues grew from the early 1960s until the mid-1970s — by 2 and 8 percentage points respectively — but have remained roughly constant since.

5. Since the mid-1970s, public sector debt has grown dramatically relative to GDP. Since the early 1960s, the debt service expenditure of the federal government has risen by nearly 4 percentage points, and that of the provincial governments by 2 percentage points. an alternate way to look at the magnitude of debt servicing is to measure it relative to total public sector spending. Since the early 1960s, federal debt service spending has more than doubled as a share of all federal spending and now accounts for more than a quarter. Over the same period, provincial debt service expenditure also doubled and now accounts for an eighth.

Table 1: ***Trends in Public Sector Revenue and Expenditure, 1961–89***
(as a percentage of gross domestic product)

	Average, late Diefenbaker years, 1961–63	Middle Trudeau years, 1975	Late Trudeau years, 1981	Average, 1980s recession, 1982–84	Early Mulroney years, 1985	Middle Mulroney years, 1989
				Revenue		
Federal	15.9	18.5	18.3	17.4	17.4	18.0
Provincial[a]						
Own sources	12.0	17.2	19.7	20.8	20.5	20.4
Federal transfers	2.6	4.5	4.0	4.3	4.5	4.0
Total	14.6	21.7	23.7	25.1	25.0	24.4
All government[b]	*27.8*	*37.4*	*39.8*	*40.1*	*40.0*	*40.6*
				Expenditure		
Federal						
Programs net of transfers to provinces	12.3	14.1	12.5	14.6	14.3	11.8
Transfers to provinces	2.6	4.5	4.0	4.3	4.5	4.0
Debt service	1.9	2.2	3.9	4.5	5.2	5.7
Total	16.8	20.8	20.3	23.5	24.0	21.5
Provincial[a]						
Programs	14.4	21.5	21.6	23.3	22.7	21.4
Debt service	1.0	1.7	2.4	3.0	3.3	3.1
Total	15.4	23.1	24.0	26.3	25.9	24.5
All government						
Programs	27.8	36.1	35.0	39.1	38.4	35.1
Debt service	3.0	3.8	6.3	7.4	8.4	8.9
Total[b]	*29.6*	*39.9*	*41.3*	*46.6*	*46.8*	*44.0*
				Deficits		
Federal	0.9	2.2	2.1	6.1	6.6	3.5
Provincial	0.8	1.4	0.3	1.2	0.9	0.1
Total	*1.7*	*2.5*	*1.5*	*6.4*	*6.8*	*3.4*

[a] "Provincial" figures are actually figures for the combined provincial, local, and hospital sector.

[b] "All government" totals exceed the sum of the matching "federal" plus "provincial" rows because revenue and expenditure for the Canada Pension Plan, the Quebec Pension Plan, and certain other items are not allocated to a specific level of government.

Source: Canada, Department of Finance, "Special Report: Financial Indicators and Reference Tables," *Quarterly Economic Review*, March 1991.

- At the provincial level, attempts to break expectations of continued wage and program increases in the public sector have resulted in numerous bitter public sector strikes. Some have involved ideologically conservative administrations (for example, the Social Credit government in British Columbia in 1983), but others have pitted unions against social democratic governments (for example, that of the PQ in 1982–83 and that of the Saskatchewan NDP in 1982).

The long-term use of the federal spending power is a subtle constitutional aspect of the deficit problem. Although EPF funding has reduced price-distorting conditional grants, Ottawa has used the spending power to such an extent that interprovincial transfers have rendered provincial budgets soft. The ability (or willingness) of provincial politicians to assess the benefits and costs of their spending decisions has declined. The most extreme cases are the four Atlantic provinces, which have long relied on Ottawa for 40 cents or more of every dollar of revenue. (This statistic underestimates their dependence on Ottawa inasmuch as it ignores provincial tax revenue derived from federal transfers to individuals and corporations in the region.) At their worst, provincial finance ministers blame their budgetary problems on reductions in transfers from Ottawa and simultaneously attack Ottawa for the size of the federal deficit!

As Irene Ip rightly insists in her recent study of provincial government finance, there is an unfortunate tendency to look at the public sector deficit as primarily a federal problem, ignoring the extent to which public spending is a function of spending and taxation decisions by *both* levels of government and the fact that provincial budgets depend heavily on intergovernmental transfers.[28] In theory at least, the federal deficit could have been transformed into a surplus in most of the past 15 years by the simple (!) recourse of eliminating all transfers to the provinces.

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[28] Irene K. Ip, *Big Spenders: A Survey of Provincial Government Finances in Canada*, Policy Study 15 (Toronto: C.D. Howe Institute, 1991).

The Interactive Results

The interactive effects among the shocks and the various nationalist discourses are by now painfully obvious. A majority of ROC Canadians plus anglophone and allophone Quebecers want the Charter of Rights and Freedoms to prevail over the Quebec National Assembly in determining language policy; most Québécois do not. Francophones outside Quebec and allophone ethnic minorities want the Charter to prevail in general over governments in defining minority rights. Populist nationalists advocate an "unhyphenated Canadianism" and are suspicious of the Charter's application to multicultural policy. Québécois nationalists and aboriginal leaders converge in not wanting the Charter to have precedence over their respective "distinct societies"; they vehemently diverge inasmuch as the latter want Ottawa to prevent any autonomous Quebec state from seceding with its present borders, which include large Northern territories primarily populated by aboriginal peoples.

Populist nationalists favor extension of the Charter to protect private property. They expect a reformed Senate to monitor and constrain federal spending; they intensely dislike the idea of a powerful social charter's dictating the level of social services and of Ottawa's having access to an unconstrained spending power. Underlying the demands for a Triple-E Senate is the concept that all provinces be treated as constitutional equals, a concept that is anathema to Québécois nationalists but has some appeal to the charter nationalist coalition, which wants to restrain provincial discretion in the area of social policy.

Supporters of a social charter are suspicious of, if not opposed to, an elected Senate for precisely the same reason its advocates want it. Social charter advocates also want Ottawa to preserve its powers to spend in areas of provincial jurisdiction so it can launch new nationwide social programs in areas such as child care. Québécois nationalists mistrust an elected Senate, the federal spending power, and a social charter as indirect means whereby Ottawa could intrude on Quebec's legislative jurisdiction.

Finally, the business community and the populist nationalists in the West clearly favor proposals to strengthen the domestic common market within Canada. Québécois nationalists and charter nationalists converge in criticizing these proposals as constraints on the scope for political intervention.

Drawing Lines in the Constitutional Sands

A country's constitution is a meta-political contract in that it establishes rules for the conduct of politics. It also serves as a lofty general statement of shared goals that define (at least in part) the nature of national citizenship. The "Canada clauses" contained in the federal proposals of September 1991[29] and the Beaudoin-Dobbie report of February 1992[30] are perfectly reasonable attempts at expressing a set of goals on which the overwhelming majority of Canadians would doubtless agree.

Yet our present constitutional crisis illustrates that reasonable people can disagree passionately as to the means most appropriate to realize shared goals — by the federal government, by the provincial governments, by the two acting jointly, by a third level of native-controlled government, by the courts acting in an expanded role — and disagree with equal passion on how best to monitor government performance. Academic constitutional experts are no different, although they have sublimated the passions of the street into a (sometimes scholastic) body of work dealing with both the positive and normative aspects of constitutionmaking.

At the risk of drastic oversimplification, one can organize discussion of the issues around the drawing of two lines in the constitutional sands, plus a look at the role of the courts and the Senate in providing checks and balances to ensure that these lines are respected. Although the sands obviously shift with time, and every generation will find itself redrawing, it is always necessary to draw these lines:

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[29] Canada, *Shaping Canada's Future Together: Proposals* (Ottawa: Supply and Services Canada, 1991) section 7. Hereinafter, "the federal proposals." For convenience, these proposals are reprinted in an appendix to this paper.

[30] Canada, Parliament, Senate and House of Commons, Special Joint Committee on a Renewed Canada, *Report*, chaired by the Hon. Gérald A. Beaudoin and Dorothy Dobbie (Ottawa: Supply and Services Canada, 1992), pp. 68–69 and 116–117.

- A line between those matters defined as individual justiciable rights enforceable by the courts and those matters subject to legislative intervention by elected parliaments.
- A line establishing provincial and federal jurisdictions and those matters subject to joint federal-provincial action.

Deciding on the appropriate placement of each is at the heart of the present constitutional debate.

The Courts and the Legislatures

The first line is essentially between the polis and civic society. Every constitution must make this division, and it will always entail controversy. A topical example is tobacco advertising. The Quebec Superior Court ruled in 1991 that federal legislation to ban tobacco advertising is an infringement on the right to free speech of tobacco manufacturers.[31] The counterargument is that government has a legitimate role in discouraging consumption because tobacco consumers, particularly young smokers, are subject to myopia and do not adequately assess the long-run health costs of tobacco addiction. The point here is not to debate civil liberties versus the importance of myopic behavior in the market for tobacco products[32] but to realize that we are constantly drawing the line between that which is legitimately subject to political intervention and that which is not.

The growth of conflicting nationalist movements in the country has exacerbated the problem of drawing this line. Frustration with elected politicians has prompted many in ROC to advocate shifting the line so as to restrict the amount of freedom given elected politicians. Many in the charter nationalist coalition, for example, want to extend justiciable rights into the domain of social policy; many in the populist nationalist coalition want to extend the Charter to a defense of private property. Others want to eliminate or restrict the Constitution's "notwithstanding" clause (section 33).

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[31] *The Globe and Mail* (Toronto), July 27, 1991.

[32] In this case I strongly favor the latter over the former argument and trust the Supreme Court, on appeal, will reverse the decision.

The traditional argument in favor of entrenched legal rights is a negative theory of human liberty: Liberty means rights that protect individuals from coercion by others, whether acting individually or collectively via the state. An entrenched charter renders rights more visible and gives enhanced legitimacy to the courts in the ongoing task of preventing such coercion. I am sympathetic with that argument. I am much less sympathetic with the extension of rights proposed by, on the one hand, advocates of a social charter and, on the other, advocates of entrenched property rights.

Most, though not all, advocates of a social charter are attempting to translate the positive role of the state into the language of rights. Positive state intervention — to redistribute income, to undertake social insurance programs, to correct fundamental market failures — is vitally important to modern society. But if such action is to be efficient, governments must enjoy a degree of freedom in designing and implementing programs analogous to that required by private firms to realize the productive potential of a market economy. The basic guarantee of preservation and improvement of the modern welfare state must be the democratic will of the majority of the country's citizens, not the will of the courts.

Similarly, the basic guarantee of the use and enjoyment of private property should lie in the majority's favoring a market economy. A justiciable right to private property invites the courts to usurp the government's legitimate role in the economy. Competitive markets are wonderfully efficient institutions when well organized, but advocates of entrenched property rights weaken the pro-market case by overstating it. A range of market failures — such as market transactions' external effects on nonconsenting third parties — creates the potential for government intervention to enhance market efficiency. Furthermore, a measure of redistribution from rich to poor is a constitutionally important goal, and such redistribution inevitably entails some subtraction from property owners' freedom to enjoy the fruits of their assets.

Centralization and Decentralization

The placement of the line between federal and provincial jurisdiction depends on the relative weight constitutional framers place on the arguments for centralization and decentralization. Let us examine each in turn.

The Case for Centralization

In brutal summary, the arguments for centralization are:

1. To realize scale economies in the production of public goods. For example, generating national defense via one army is cheaper per capita than via ten armies. Accordingly, it was appropriate for British Columbia to give up the submarines it had purchased before World War I. Tax regulations afford a second, less whimsical example. It is more efficient to have one set of forms than eleven. In general, Ottawa should define income and sales tax regulations and the provinces should vary only the rates on taxes within their jurisdiction.

2. To avoid policy spillovers (externalities between jurisdictions). For example, if a province can import skilled labor trained elsewhere, it may stint on expenditures on postsecondary education and labor training. Thus, interprovincial mobility provides a rationale for federal jurisdiction over these functions.

3. To lower the uncertainty of government revenues. The economy of the nation comprises a larger number of industries than does the economy of any one province. The markets for various industries are somewhat independent of one another; when some industries are depressed, others are thriving. Of course, recessions affecting virtu-

ally all industries do occur, but even then some industries are less affected than others. Thus, the variability of national per capita income is likely to be lower than the variability of any particular province's per capita income, and Ottawa can realize more stable revenues at constant tax levels than can any province.

4. To avoid inefficient mobility — or lack of mobility — of labor and capital resulting from the provision of different levels of income distribution by different provinces. The altruism of citizens in all societies prompts some redistribution of income from rich to poor. Modern secular societies organize this redistribution primarily via the state. The question is which level of a federal state can undertake the exercise most efficiently. If a provincial government — say, that of Alberta — is very generous in subsidizing investment, it can create an inefficient pattern of industry. If another provincial government — say, that of Saskatchewan — is very generous in subsidizing farmers, it retards the efficient movement of labor out of agriculture. Centralized redistribution is more likely to avoid encouraging inefficient migration of capital and labor.

Notice, however, that this argument holds only for public policy that is purely redistributive. Publicly provided social insurance programs should not be equated with income redistribution.[33] Although the former frequently entail a measure of redistribution from rich to poor, they are primarily a social contract whereby ordinary citizens oblige themselves to buy insurance in preparation for old age or against unexpected unemployment or ill health. Redistribution is income transfer to those who are currently poor, are expected to remain so for long periods, and have not entered a contract to buy social insurance via tax payments.

5. To avoid destabilizing "games" between provinces. This problem is less acute for Canada than for some other federations — consider, for example, the escalating tit-for-tat violence between Croats and Serbs. Canadians have, however, played similar if less murderous

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[33] See Jean-Michel Cousineau in this volume.

games by, for example, escalating provincial barriers against interprovincial trade in agricultural products, beer, and other commodities.

6. To retain a balance of dual loyalties. If provincial governments are the primary providers of social services and in peacetime the locus of the largest part of public spending, there is a danger that citizens will cease to be interested in the shared aspects of citizenship that transcend provincial loyalties. Many advocates of the Charter of Rights and Freedoms defended Ottawa's introduction of it as a means of filling what they perceived as a lack in the shared identity of being a Canadian.[34]

The Case for Decentralization

In equally brutal summary, the arguments for decentralization are:

1. To encourage policy innovation by intergovernmental competition. This case is analogous in many ways to the case for competitive markets over central planning. Decentralization within a federal state encourages competition in politics. An important characteristic of competitive markets is simply the potential they afford for experimentation. Many market innovations do not prove efficient and the innovators fail financially; others, however, succeed and become widely adopted. At any given point, the market may appear chaotic as different firms do things in different ways in a context of uncertainty. The analogue to this creative anarchy of entrepreneurial innovation in the market is political entrepreneurs' running different provincial governments and attempting to win popular support by introducing new programs.

2. To allow a closer match between public policies and citizen preferences. The most important application of this argument is to

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[34] See, for example, A.C. Cairns, "Constitutional Change and the Three Equalities," in R.L. Watts and D.M. Brown, eds., *Options for a New Canada* (Toronto: University of Toronto Press, 1991).

language policy. As already discussed, preferences in ROC and Quebec differ drastically. Decentralized jurisdiction over language, subject to entrenched minority language rights, would satisfy more people than any single policy pursued by Ottawa.

3. To lower citizens' costs of signaling preferences. One advantage a competitive market with many sellers has over a centrally planned economy is that consumers in the former face far lower costs in indicating their desired quantity and quality of particular goods and services. A particular group of consumers unhappy with the existing offerings need persuade only one seller to change. Analogously, a group of citizens unhappy with a locally provided public good or service need persuade only one government to change. In general, citizens face lower costs in signaling their preferences if the relevant government is local.

4. To create more encompassing interest groups and reduce "rational ignorance." Interest groups weigh the costs of bargaining against the expected gains; the latter must exceed the former before bargaining occurs. Successful interest groups tend to restrict their membership and define narrow goals because: (1) the costs of a lobby rise with the number in it; (2) the narrower the goal, the lower the cost of reconciling potentially divergent aims among members of the lobby; and (3) large size brings with it the problem of controlling free riders who cannot easily be denied a share in the benefits gained even though they have not contributed actively to the lobby. Moreover, a lobby is less likely to provoke organized opposition if the costs of realizing its goals can be diffused over a large number of people for whom formation of a counterlobby would be prohibitively expensive. Thus, politics tends to generate policies that confer concentrated benefits on narrow interest groups and diffused costs borne by a large population.

Decentralization diminishes the problem. An interest group of a given size is necessarily larger — more "encompassing" to use

Mancur Olson's term[35] — relative to a province than to the national economy. The more encompassing an interest group, the more willing its leaders will usually be to consider the inefficiencies arising from its lobbying activity — because its members are more likely to incur some of those costs. Furthermore, the larger the per capita cost imposed on the population, the more likely that over time a counterlobby will form to oppose the interest group's inefficient rent-seeking.

Lobbying (and counterlobbying) is costly, but so is learning about the costs and benefits of alternate public policies. Citizens will rationally remain ignorant unless the per capita benefit of government's adopting an alternative policy — multiplied by the subjective probability that the citizen intervention will affect the policy choice — exceeds the cost of learning about the matter. Perhaps the most inefficient set of Canadian public policies, in terms of lost potential economic gains, are those pursued by the federal Department of Fisheries. One reason for the persistence of such inefficiency over decades is rational ignorance. How many voters in Toronto are aware of the costs to them of federal fisheries policy? Rational ignorance can also impede the improvement of provincial policies, but the costs of learning about local matters are lower and the per capita benefits of an equal dollar improvement in public policy are greater.

Checks, Balances, and Monitors

Instruments to check, balance, or monitor the exercise of political authority exist because of mistrust. The greater popular mistrust of politicians, the more significant become the demands for such checks. Canadians are highly mistrustful in this time of constitutional disequilibrium and not surprisingly the demand for enhanced checks and balances is a major component of the constitutional agenda.

Two issues need to be addressed here briefly. First, enhancing the monitoring function may expand the influence of interest groups opposed to budgetary restraint relative to the influence of groups that favor it. The reason lies with the interest groups' unequal potential for organizing. Well-organized interest groups tend to define narrow goals of benefit to a special constituency. Groups pursuing diffuse goals that would favor a broad constituency suffer from free-rider problems and are usually less well organized. Advocates of any particular public expenditure typically constitute a narrow group; opponents unwilling to pay for the expenditure are usually a diffuse, ill-organized group. This dynamic generates unequal pressure on all political agents. The requirement of financial accountability limits interest group influence on elected members of a government. Monitoring agents — judges or senators — do not, however, face the same constraint of financial accountability and are therefore more likely to succumb to the temptation to act as agents of well-organized interests.

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[35] M. Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation and Social Rigidities* (New Haven, Conn.: Yale University Press, 1982).

In the long run, the use of monitoring institutions to relax budgetary constraints is self-defeating for the very interest groups that undertake such activity. If taxpayers do not receive value for money, they ultimately engage in a generalized rejection of public programs. The protest against the GST and the rise of the Reform Party, which argues the right-wing case against "big government," are early manifestations of such a taxpayers' revolt.

The second issue is the relative advantage of monitoring via justiciation in the courts or via a second legislative chamber. Courts are good at drawing complex lines through a multitude of factors bearing on individual cases and thus at enforcing negative concepts of liberty that require constraints on the state's ability to infringe fundamental individual rights. The market analogy is that courts are efficient monitors of behavior governed by formal contracts between individuals.

Courts are, however, generally inefficient at monitoring the positive functions of the state in the provision of public goods and services and in the redress of market failures. A well-functioning Senate is probably a more efficient monitor of public policies that impinge on individuals via their membership in collective institutions. To continue the market analogy, a well-functioning Senate can play a role like that of an association of trade unions or of firms in a particular industry, and represent the collective interest of constituent collectivities.

Nine Recommendations

This section proposes nine constitutional changes. None of them is novel; all have figured in the reports of Royal Commissions, the platforms of political parties, and the writings of academics and journalists over the years. Yet construction of one or more set of constitutional proposals has, I hope, some value — if only to aid the reader in evaluating the proposals that will ultimately emerge from the process of intergovernmental negotiations under way at time of writing (May 1992).

I have divided my proposals into two groups — the necessary and the highly desirable — using a straightforward rationale. Given the fracturing of Canadian political discourse into four conflicting nationalisms over the past quarter century, the highest priority for constitutional reform must be to realize a compromise that satisfies the rational core of the demands articulated by each of the nationalist communities:

- Acceptance of the legitimacy of the Quebec government's role in promoting French within the province.
- Acceptance of a third, aboriginal-controlled level of government that will guide native Canadians' collective adaptation to life in an industrial society.
- Acceptance of an elected Senate that will provide the smaller provinces with a means of effectively monitoring the performance of the central government.
- Acceptance of a modest social charter that states our collective commitment to high-quality public services and provides a mechanism to monitor the performance of both the federal and provincial governments in providing them.

Unless we find accommodation on these four matters, it will probably prove impossible to secure popular acceptance of any constitutional package.

The primary motive for my other five recommendations is a concern to preserve the ability of provincial governments to act efficiently and independently and to be accountable to their electorates for those functions over which they have jurisdiction. The net effect of these five recommendations is somewhat decentralist, although the recommendation on the economic union would impose an important limit to provincial discretion.

Necessary Reforms

Recommendation 1: Language

> *Quebec should enjoy constitutional legitimation of its policies to promote French within the province. If a majority of Canadians in both Quebec and ROC accept a "distinct society" clause, then we should adopt it. If the majority in ROC continue to reject it, then we should substitute the more explicit recommendation of the Pepin-Robarts report: that, subject to entrenched minority language rights, each provincial legislature be able to declare an official language or languages within its respective jurisdiction. Ottawa should continue to maintain the equality of the two official languages within the federal jurisdiction.*

As discussed earlier in this paper, individuals' choice of language is significantly influenced by expected net benefits, and the choice of a particular language by one group has external effects on the language choices of others. Given these economic factors in language choice, the French character of Quebec in general and of Montreal in particular cannot be guaranteed if the choice of the language of instruction and of work is treated as a civil liberty. The Québécois are understandably insistent that the Constitution legitimize their language laws, which have, over the last generation, buttressed the official status of French and restricted the use of English.

Like the Meech Lake Accord, the federal proposals of September 1991 and those of the Beaudoin-Dobbie report of February 1992 attempt this legitimation by resort to the "distinct society" concept introduced by the Beige Paper in 1980. If a majority of Québécois and Canadians in ROC accept this approach as a satisfactory compromise, then we should adopt it.

The "distinct society" clause was, however, probably the principal cause of popular hostility to the Meech Lake Accord in ROC. (Why should the Constitution declare Quebec to be a society more distinct than any other in the country?) Two recent polls suggest that hostility is still present. According to one poll conducted by *The Globe and Mail* and the CBC, 63 percent within ROC oppose introduction of the "distinct society" clause, and only 28 percent approve; within Quebec, the proportions are almost exactly reversed; with 63 percent approving; 29 percent opposing. A *Maclean's*/Decima poll found much the same situation: 69 percent in ROC oppose introduction of the clause and 28 percent approve; in Quebec, 77 percent approve and only 20 percent are opposed.[36]

If these public attitudes persist and harden, we should resurrect the more explicit allocation of language jurisdiction recommended by the Pepin-Robarts report. Given the extent of linguistic mistrust at present, minority linguistic rights should, however, remain within the Constitution and not be, as proposed by Pepin-Robarts, in the form of provincial statutes. It is also important to emphasize that the designation of an explicit provincial domain of language jurisdiction would in no way preclude Ottawa from pursuing bilingual policies within its jurisdiction. Indeed, both reports explicitly advocated constitutional entrenchment of a set of bilingual rights within federal jurisdiction.

An explicit provision for provincial jurisdiction over language would, polls suggest, satisfy the majority of Québécois. It would also probably be more acceptable than "distinct society" in ROC. As a secondary benefit, designating a domain of provincial language would encourage the ROC provinces to pursue language policies better adapted to their respective linguistic circumstances. These policies might range from continuation of official bilingualism in New Brunswick, to better Ukrainian courses in Prairie schools, to better services in Cantonese and Punjabi in British Columbia.

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[36] The polls were reported respectively in *The Globe and Mail* (Toronto),November 4, 1991, and *Maclean's*, January 6, 1992.

Recommendation 2: Aboriginal Rights

> *The Constitution should be amended to include, both in the body and in the "Canada clause," reference to the inherent right of aboriginal Canadians to self-government. In addition, aboriginal Canadians should become one of the constituencies electing members to a reformed Senate.*

The problems of aboriginal Canadians have dramatically intruded into the discussion of division of powers during the past decade because the central aboriginal demand is for a new level of government — one independent of both federal and provincial jurisdiction. The federal government in 1991 established the Royal Commission on Aboriginal Peoples, headed by George Erasmus, former head of the Assembly of First Nations, and Judge René Dussault, of the Quebec Court of Appeal. It is to be hoped that the establishment of this Royal Commission signals a higher priority at all levels of government for aboriginal problems than has been evident heretofore.

It is clearly essential that aboriginal Canadians be recognized in a revised Constitution. Moreover, it should be accepted that this third level of government arises from these peoples' *inherent* right to self-government, not from delegation from the federal and provincial governments. The Royal Commission recently published a commentary strongly supporting this argument: "Aboriginal peoples are the heirs to ancient and enduring powers of government that they brought with them into Confederation."[37]

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[37] Canada, Royal Commission on Aboriginal Peoples, *The Right of Aboriginal Self-Government and the Constitution: A Commentary* (Ottawa: Royal Commission on Aboriginal Peoples, 1992), p. 18.

Interpretation of this inherent right will, it must be emphasized, pose many problems. As the commissioners themselves recognize, this third level of government must be "circumscribed rather than uncircumscribed in its extent."[38] Aboriginal rights to self-government do not extend to full sovereignty, so the division of powers must be clarified in the future. Are aboriginal governments to be bound by the Charter of Rights and Freedoms? The Assembly of First Nations replies no, but native women's organizations say yes. Who is to be subject to aboriginal governments? Should their authority extend, for example, to Métis and other aboriginals not defined by the *Indian Act*? Should it be exercised solely over natives living on reserves, or should it extend to off-reserve aboriginals? Given the low employment level of aboriginal Canadians and their consequent small tax base, how would the new governments finance their activities? If they remain almost entirely dependent on transfers from white-dominated federal and provincial governments, can they really exercise autonomy?

Despite these difficult unresolved questions, it is important that we signal a willingness to experiment free from the restrictive traditions of the *Indian Act*. Other countries have evolved a range of self-government traditions for their aboriginal peoples that are worth exploration. An obvious example is the U.S. approach of treating native governments as "domestic dependent nations" with some lawmaking and judicial autonomy from both state and federal government.

Of less importance but worthy of support is the federal recommendation proposing aboriginal representation in a reformed Senate (see my Recommendation 3).

Recommendation 3: A Double-E Senate

> *The Senate must become, like the courts using the Charter, an effective monitor on the performance of the federation. In order for it to perform this function, its members should be elected. Ideally, the Senate should have equal representation from six*

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[38] Ibid., p. 20.

> *constituencies: Atlantic Canada, Quebec, Ontario, the Prairies plus the Northwest Territories, British Columbia plus the Yukon, and the aboriginal peoples.*

The proposal most discussed has been a Triple-E Senate — one that is elected (directly by Canadian citizens), equal (in number of senators per province), and effective (in its ability to control federal government actions). The most ardent advocates of such a Senate have been the governments of some of the smaller provinces — most notably Alberta and Manitoba in the West and Newfoundland in the East — and the Reform Party.

There can be few objections to the first E; any reformed Senate must be elected if it is to exercise legitimate authority. It is doubtful, however, that the chamber should be more than "half equal" or "half effective."

To most proponents, the second E stands for provincial equality in the number of senators. The symbolic meaning of this proposal is to affirm the importance of the peripheral provinces and the constitutional equality of all provinces. To be blunt, this symbolism is undesirable. Different provinces have dramatically different administrative capacities, and their citizens display markedly different preferences with respect to various public policies (most notably language). Our constitutional need is to *accommodate* unequal provincial attributes, not deny them.

The undemocratic aspect of defining equality in terms of an equal number of senators per province also deserves attention. If this definition were accepted, an Ontario senator would represent 73 times as many people as one from Prince Edward Island. More important, the concentration of small provinces in Atlantic Canada would impart an acute regional imbalance: the 29 percent of Canadians in the four Western provinces would have 40 percent of the vote, as would the 9 percent in Atlantic Canada; the 37 percent in Ontario and 25 percent in Quebec would each have 10 percent.

In general, the more the electoral formula approaches equality of provincial representation and the further it deviates from representation by population, the less willing will be the larger and wealthier provinces to accept meaningful Senate reform. Even if Alberta favors a Triple-E Senate, the two other "have" provinces, Ontario and British Columbia, do not. Finally, Quebec will inevitably fear a Triple-E Senate as an indirect means of offsetting any gains in jurisdiction obtained elsewhere in the constitutional reform process.

An effective and elected monitor would, however, be potentially useful constitutional reform. Courchene has proposed what may be the appropriate "half E" for equality,[39] a compromise I recommend with slight modification: Divide the country into six constituencies, each of which would elect an equal number of senators. The first constituency would include those who choose to define themselves as aboriginal Canadians. The remaining five would be regionally based: Atlantic Canada, Quebec, Ontario, the Prairies plus the Northwest Territories, and British Columbia plus the Yukon.

We must be just as careful in defining the E for "effective." The matter is already confused. Popular support for a Triple-E Senate began as a populist response to the NEP, a set of policies rightly criticized in Western Canada as inefficient subsidies to the large number of voters in Ontario and Quebec at the expense of the small number of voters in Western resource-rich provinces. A Triple-E Senate would, its proponents argue, prevent the repetition of such policies. Triple-E advocates in Atlantic Canada have extended the argument in an altogether different direction. They perceive such an institution as a guarantee against future, more economically efficient federal policies that would limit federal transfers to their region.

In pursuing these contradictory concepts of effectiveness, Triple-E advocates lose sight of the prime function that a reformed Senate should pursue: effective and legitimate monitoring of government activity. In addition to monitoring the federal government, a reformed Senate could be a watchdog on the performance of provincial governments in the provision of social services and on joint federal-provincial decisionmaking about the economy and the environment (see Recommendations 4 and 6).

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[39] Courchene, *The Community of the Canadas.*

It is appropriate that legislation require approval by both the Senate and the House of Commons. But if the Senate rejects a particular bill and, after the attendant public debate, the Commons reaffirms its majority decision, the Senate should not be able to block the matter further. We should be wary of making the federal government accountable to two chambers, which would be the case if the Senate enjoyed more than a suspensive veto. Accountability to two masters poses the disadvantages of the congressional system in the United States: that government end up accountable to neither the executive nor the legislative branch. Canadians need a federal government that displays as much efficiency, autonomy, and accountability within its jurisdictions as do the provinces within theirs. Given concerns of Western advocates of Senate reform about past inefficiencies in Ottawa, they should be among the people most wary of an overly effective Senate that serves to prevent future reform of inefficient federal transfer programs.

If Québécois demands for provincial control of language are met by an explicit allocation of this matter to the province, then the potential influence of the Senate over language becomes less important. If, however, we adopt the more ambiguous "distinct society" clause, then it would be desirable to limit potential Senate intrusion in the area of language by a double-majority voting procedure, as suggested in the federal proposals. Provincial control of resources plays in Western Canada a role somewhat analogous to provincial control of language in Quebec. In order to convince Western Canadians that there will be no repetition of the sins of the NEP, it may be useful to apply a double-majority voting rule to federal laws bearing on resource management.

Recommendation 4:
A Modest Social Charter

> *Part III (Equalization and Regional Disparities) of the* Constitution Act *should be extended into a modest social charter. Ottawa and the provincial governments should entertain two additional commitments: managing public services to support*

> *the retraining and mobility of workers whose employment is endangered by changes in market conditions or by implementation of proposals to enhance the domestic common market; and pursuit of sound environmental policies. Furthermore, the Senate should play a monitoring role by reporting annually to Parliament and to the legislatures of the provinces on the quality of essential public services and environmental policies provided by the respective governments.*

Elsewhere I have proposed a modest social charter[40] based on extending the part of the *Constitution Act* that currently commits Ottawa and the provincial governments to "providing essential public services of reasonable quality to all Canadians" and to "the principle of making equalization payments." I would add two more commitments: to retraining and supporting the mobility of workers who are threatened by changes in market conditions or an enhanced interprovincial market, and to pursuing sound environmental policies. In addition, my proposal would have the Senate monitor the quality of essential public services and environmental policies provided by the federal and provincial governments.

The rationale for a social charter — in addition to the *realpolitik* of accommodating the charter nationalist coalition — is twofold. First, the provision of generous, European-level social services has become a broadly shared goal of Canadians, one sufficiently important to merit constitutional recognition. But providing these services falls primarily to the provincial governments. There is a real danger that a social charter would blunt the accountability of provincial governments for the efficient management of expenditures within their jurisdiction. Accordingly, any proposed social charter should emphasize the function of monitoring government performance: publicizing the good and condemning the bad. It should, however, stop short of current demands for a full-blooded social charter that would allow either the courts or some joint federal-provincial institution to dictate the content of social programs.

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[40] Richards, "A Social Charter: Two Cheers but Not Three."

The second rationale for a social charter derives from the idea that commitment to the principle of universal retraining and mobility programs would be an appropriate constitutional balance to the acceptance of other proposals that would free the domestic market from trade barriers. (This idea is developed further in discussion of Recommendation 8.)

Highly Desirable Reforms

Recommendation 5: Clarification of Provincial Jurisdiction over Basic Social Services

> *Section 92(7) of the* Constitution Act *should be revised to state that, subject to the power of delegation and a modest social charter (see Recommendation 4), the provinces have jurisdiction over the planning, financing, and management of basic social programs of health insurance and social assistance. Ottawa should continue its responsibility for pensions and other transfers to individuals that rely on the income tax system.*

One of the conclusions to draw from the historical survey earlier in this paper is that Canada developed its good social services on a basis of two principles: creative exercise of provincial jurisdiction, and interregional transfers to permit reasonably comparable services across the country at reasonably comparable taxation rates.

But what of the future? Some Canadians are anxious that provincial governments are allowing unwarranted increases in social service expenditures, which in turn are exacerbating public sector deficits. Others fear that in constraining the growth of social service spending, provincial governments are destroying national standards. My basic conclusion is *plus ça change, plus c'est la même chose.* Controversy has surrounded social program spending throughout much of this century and will probably continue into the next.

In general, here is a domain of public sector spending to which the decentralist arguments of the previous section should apply. The primary guarantee of our social services should be that Canadians, in their capacity as citizens of their respective provinces, want to maintain and improve them, are prepared to pay for them provided they get value for money, and would penalize provincial politicians that destroyed them.

Consider, for example, the recent history of Canadian health insurance. When some provinces allowed physicians to bill patients for amounts in excess of payments from the provincial health insurance programs, Ottawa enacted the *Canada Health Act* of 1984. It imposed financial penalties on provinces whose health programs violated "national standards" stipulated in the act. The unintended effect has been to raise the political cost to provincial governments of maintaining financial accountability since the act affords frustrated provider groups standing to appeal to Ottawa against provincial decisions. A recent example was the Quebec government's saying it would impose a user fee on nonemergency use of hospital emergency wards in an attempt to divert such patients toward less costly community health centers. Such a fee would be in technical violation of national standards, and MPs from all parties called on Ottawa to invoke the financial penalties stipulated in the *Canada Health Act*.[41] At time of writing, the fee had yet to be imposed, but the point is obvious. The emergence of national standards increases the difficulty of provincial budgeting.

Key to the success of the Canadian model of health care insurance is that provincial governments act as the sole agent representing health care users (provincial residents) in effective bilateral bargaining with health care provider groups. To cite a prominent Canadian health economist: "The critical feature of the Canadian system is that provincial governments cannot slide away from their financial responsibility for virtually all hospital and medical care funding. They have no option but to engage in the difficult and politically dangerous process of compression."[42]

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[41] *The Globe and Mail* (Toronto), December 8, 1990.

[42] R.G. Evans, "Tension, Compression, and Shear: Directions, Stresses, and Outcomes of Health Care Cost Control," *Journal of Health Politics, Policy and Law* 15 (1990): 119.

This bilateral monopoly model has served Canadians well. It has allowed Canada better epidemiological health results at lower cost than the United States.[43] During the 1980s, the Canadian provinces stabilized the proportion of GDP devoted to health care costs, whereas the Americans, relying on more individual user fees and multiple paying agents, did not. Comprehensive provincial reviews, such as the recently completed study of the British Columbia Royal Commission on Health Care Costs,[44] offer the best means for balancing benefits and costs and maintaining public sector accountability. By reducing accountability, the imposition of national standards endangers the value for money Canadians currently receive for their health taxes. The successful provincial management of health and other basic social services does, of course, require predictability in federal transfers. For that reason, Ottawa should enter into long term — say five-year — agreements that it does not unilaterally amend. The Beaudoin-Dobbie Committee responded to recent unilateral federal reductions in intergovernmental transfers by proposing a constitutional amendment to the effect that henceforth such agreements would prevail over any future government legislation. Such an amendment might be workable, but it would complicate the constitutional division of powers and cover what should be part of the administrative conventions of federal-provincial relations.

Despite the importance of maintaining provincial accountability and jurisdiction, the federal government obviously has played and should continue to play a role in social policy beyond interregional transfers. This role is particularly evident in programs built around the income tax system, such as tax credits for low-income earners, in which scale economies give Ottawa a comparative advantage. Another example is old age pensions, a domain of the welfare state for which most initiatives have originated in Ottawa since the

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[43] As of 1989, Canada devoted 8.9 percent of GDP to health care expenditures, the United States 11.6 percent. See United States, General Accounting Office, *Canadian Health Insurance: Lessons for the United States*, GAO/HRD-91-90 (Washington, D.C., 1991), p. 14.

[44] British Columbia, Royal Commission on Health Care and Costs, *Closer to Home* (Victoria: Government of British Columbia, 1991).

1920s. (This fact was recognized by the 1951 constitutional amendment making pensions a concurrent jurisdiction.)

In sum, "if it ain't broke, don't fix it." Rather than recommend a powerful social charter or provision for joint federal-provincial jurisdiction, I suggest merely an updating of the antiquated language of section 92(7) of the *Constitution Act*, the section that makes health care and social assistance an exclusive provincial jurisdiction.

Recommendation 6: Promotion of the Canadian Economic Union and Protection of the Environment

> *In general, both levels of government should be jointly responsible for promotion of the economic union and environmental protection. The Senate should play a major role in monitoring this joint federal-provincial exercise of jurisdiction.*

Both economic management and environmental policies display significant spillover effects (externalities), and thus the initial presumption is that jurisdiction for both should be centralized. Such an allocation would, however, raise at least three difficulties. First, a very large proportion of government activities can be interpreted as having an economic or environmental aspect (or both), and hence a broad interpretation of federal jurisdiction in these areas would extinguish many domains of provincial jurisdiction.

Second, it is important to realize that historically *both* levels of government have been equally guilty of offenses in matters of environmental and trade policy. Provincial offenses to internal free trade are obvious. They include acts and regulations that limit the interprovincial mobility of skilled workers and professionals, restrictions on interprovincial trade in agricultural goods (conducted under federal enabling legislation), inefficient provincial procurement policies, and the imposition of other nontariff barriers. (The most infamous outcome of the last is perhaps the provincial "beer fiefdoms" of small, inefficient breweries across the country.) The most important federal offense is unemployment insurance. Since premiums do not reflect the inherent unemployment risk of different industries, the program acts as a subsidy to high-risk, seasonally cyclical industries such as fishing, construction, and forestry. Moreover, Ottawa has added various income-subsidy schemes (such as fishermen's benefits) that have further eroded the concept of the program as insurance against unemployment. Both levels of government are also guilty of failure in environmental protection. For every environmentally dubious dam sponsored by British Columbia, Saskatchewan, and Quebec, there is an environmentally dangerous offshore oil project that proceeds only with federal subsidy. If both levels of government are foxes, is it sensible to entrust the chicken coop to one of them?

Third, some economic and environmental policies display few spillovers, and a decentralized jurisdiction allows the benefits of intergovernmental competition. For an illustration, consider the recent conversion of many power utilities to the pursuit of energy conservation. Here, as in many earlier cases of emerging public policy, intergovernmental competition is creative. Power utilities in both Canada and the United States, plus their respective provincial and state regulatory bodies, are engaged in a chaotic but productive competition among themselves. With the Western states from California to Washington facing acute electrical shortages, their regulatory bodies have encouraged demand-side management by redesigning regulations to allow utilities to earn profits from investments that *reduce* demand. In Canada, B.C. Hydro has pioneered the adoption of demand-side management techniques, but other provincial utilities have launched their own programs.

Given the disadvantages of an exclusive federal or provincial exercise of jurisdiction in these areas, economic management and the environment are candidates for joint federal-provincial jurisdiction. There exist many proposals for concurrent jurisdiction, in economic management in particular. Before we examine them, it is useful to distinguish between provisions for negative and for positive economic integration. The former are self-denying edicts on the part of governments not to interfere in the free movement of goods, services, labor, and capital. The latter refer to positive government actions intended to improve market efficiency — such as regulations to assure a common currency, programs to develop transportation infrastructure.

If we make this distinction, several questions arise. With respect to negative economic integration, what institution will enforce it? With respect to positive integration, what institution has the power to initiate such legislation? And what institution, if any, has the right to ratify or to monitor it? With respect to both positive and negative integration, can governments grant themselves exemptions in particular instances?

Using the distinction between negative and positive integration and these four related questions, let us consider several options that have recently been advanced.

Option A: Positive integration, federal proposals.[45] A new section 91A would specify that Parliament may initiate laws "it declares to be for the efficient functioning of the economic union," but legislation under this head would not have effect unless approved by seven provinces comprising at least 50 percent of the Canadian population (the "7–50 rule"). The proposal contains a limited provision for individual provinces to exempt themselves from any particular initiative. As this proposal stands, it is not acceptable to most provinces, including Ontario and Quebec; too much initiative lies with Ottawa.

Option B: Negative integration, federal proposals.[46] The present negative integration clause (section 121) refers solely to goods; it makes no reference to trade in services or to the mobility of labor or capital. The federal proposal would make that extension. However, this particular proposal has the disadvantage of multiple escape hatches. It would not apply to any law of Parliament intended to further equalization or regional development. It would not apply to most provincial laws that could be construed to advance regional equality within the province. It would not apply to a law of Parliament or of a provincial legislature if declared to be in the "national interest" under the 7–50 rule.

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[45] The federal proposals, section 15.

[46] Ibid., section 14.

Option C: Positive integration, Leslie.[47] In a document released simultaneously with the federal proposals, Peter Leslie analyzed the functioning of the European Community (EC). He is, in general, favorably disposed to the evolution of Community practice, which has increasingly emphasized positive integration measures initiated by institutions in Brussels representing both the EC as a whole and the member states. One can infer from Leslie's document a preference for a positive integration option in which initiative would be the prerogative of a joint federal-provincial body. He is not much interested in escape hatches and would like some level of the courts to play the leading role in enforcement.

Option D: Negative integration, Simeon.[48] An option much more kindly disposed than Leslie's to the potential of the provinces to promote the economic union is that of Richard Simeon. He proposes that Parliament or any provincial legislature be empowered to launch a complaint against a law of any other government on grounds it violates domestic free movement of goods, services, labor, or capital within the country. Adjudication of the complaint would fall to an intergovernmental agency, which would have the power to declare offending laws *ultra vires*.

Option E: Negative integration, Beaudoin-Dobbie report.[49] This option for updating section 121 is very similar to the negative integration option contained in the federal proposals. Like it, it contains multiple escape hatches. It would not apply to any federal law intended to further equalization or regional development, nor to any provincial or territorial law intended to reduce economic disparities within the jurisdiction. It would not apply to any federal, provincial, or territorial law enacted for "public protection, safety or health," to any Crown corporation "exercising monopolies in the public interest," or to any "marketing and supply management systems in the national, provincial or territorial interest."

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[47] Peter Leslie, *The European Community: A Political Model for Canada?* (Ottawa: Supply and Services Canada, 1991).

[48] Richard Simeon, "Some Observations on the 'Powers over the Economy'," in David W. Conklin, ed., *A Separate Personal Income Tax for Ontario* (Toronto: Ontario Economic Council, 1984).

[49] The Beaudoin-Dobbie report, pp. 121–124.

In considering what should be done in this area, we should recognize that Canadians have constructed a productive domestic market with much economic integration relying on the antiquated constitutional provisions of the *British North America Act* and a century of judicial interpretation. Thus, although reform in this area is highly desirable, it should not be pursued if the price is adamant opposition from one of the nationalist constituencies and a risk of constitutional deadlock.

With that caveat, I put forward the following options as a contribution to the debate. Like my recommendation for a social charter, they accord the Senate a major role in monitoring government compliance.

Option F: Positive integration. Initiatives could emanate from Ottawa or from a set of provinces satisfying the 7–50 rule — thereby avoiding the presumption that Ottawa alone can utilize this potentially very broad jurisdiction. The Senate would play a significant role: it would have to ratify any legislation proposed under this head, and governments that sought an exemption would require Senate approval.

Option G: Negative integration. Subsections (1) and (2) of the updated section 121 in the federal proposals are admirable statements of the principle of a domestic economic union. Disagreement centers on mechanisms for enforcement and exemptions. There is value in attempting to make all 11 governments jointly responsible for maintenance of the economic union. Accordingly, I propose Simeon's enforcement mechanism (see option D). Some additional procedure for leave to appeal to the courts might also be useful. The Senate should monitor exemptions from particular laws, and any government seeking one should have to obtain Senate approval.

With appropriate modifications, Options F and G could also apply to environmental law. On the negative side, any government could launch a complaint against another; the complaint would be adjudicated by Simeon's intergovernmental agency. The initiative for positive measures — a carbon tax is an attractive example — could be made only by Ottawa or a set of provinces satisfying the 7–50 rule. The Senate would have to endorse the measure and would rule on exemptions.

Recommendation 7: Delegation of Powers

> *Provincial and federal governments, by a resolution of their respective legislatures, should be able to delegate particular powers, for specified periods of time, to another government or to a public agency controlled by a subset of the 11 Canadian governments.*

There is a need for flexibility in the assignment and reassignment of legislative powers, a need to recognize the different administrative capacities among provinces and the different preferences among citizens across provinces and over time with respect to the desired level of centralization. Concurrency of federal and provincial jurisdiction is one mechanism to permit flexibility, but it raises many problems. Delegation is, in general, a neater mechanism to realize the same goal. Both the federal proposals and the Beaudoin-Dobbie report recommend that the Constitution be amended to permit legislative authority to be delegated, by mutual consent, from one legislative body to another.

Both delegation and concurrency run counter to the currently popular idea of symmetry among provinces. Yet even leaving aside the matter of Quebec's unique role in promotion of French culture, the principle of equal treatment of all provinces is undesirable. Different provinces have dramatically different populations, which, in turn, affect their respective administrative capacity. And local preferences differ between, for example, traditionally centralist Manitobans and traditionally decentralist Albertans. Some divergences already exist in Canadian constitutional practice — consider, for example, Quebec's opting out of the Canada Pension Plan to form its own variant.

Delegation to intermediate bodies may also be appropriate. For example, six provinces — British Columbia, Quebec, and the four in Atlantic Canada — have an interest in the ocean fishery. If the costs and benefits of fishery policy were internalized to an intergovernmental body representing only these provinces, it might be feasible to induce a more efficient outcome. Analogous arguments apply to delegating authority over the Wheat Board to the four Western provinces. If such experiments in delegation proved successful, they might encourage union of the Atlantic provinces — and even of the two smaller Prairie provinces — whose small size probably imposes high costs in the provision of some public services.

Recommendation 8: Active Labor Market Programs

> *Jurisdiction over labor training should be transferred to the provinces with provision for delegation to an agency controlled by a subset of provincial governments.*

Better programs in labor training and mobility are a necessary complement to programs to remove trade barriers. The proponents of free trade frequently overstate their case by ignoring its distributional consequences. Although well-functioning competitive markets undoubtedly enhance efficiency and usually generate net benefits, they also generate losses. A particularly important category of losses is borne by workers whose industry-specific skills are devalued by removal of trade barriers. In a pluralist democracy with powerful occupational interest groups, it is politically impossible to secure consensus on behalf of free trade without simultaneously putting in place comprehensive labor market programs that will lower the uncertainty and socialize much of the risk borne by workers with industry-specific skills.

Labor training is currently undertaken by both the federal and provincial governments; unemployment insurance has been under federal jurisdiction since a constitutional amendment of 1940. A multitude of studies have criticized the inadequacies of present policies.[50] They have all concluded that too much money is spent on "passive" programs (untied income transfers to the unemployed, primarily via unemployment insurance) and too little on "active" programs (retraining and mobility).

Here is a case in which the initial theoretical arguments appear to favor centralized jurisdiction for both activities. With respect to labor training, externalities are important because of the extent of interprovincial mobility of people. With respect to unemployment insurance, Ottawa is better placed to fund the program because it draws revenue from all sectors of the economy and therefore has a more stable revenue base than any particular province could provide. Furthermore, by standardizing premiums and benefits, Ottawa could prevent inefficient labor mobility (or lack of it). Historically, however, acute lobbying by interest groups has offset these theoretical advantages. Unemployment insurance has lost much of its rationale as an insurance program and increasingly become an inefficient supplementary system of welfare. Premiums are unrelated to risk of unemployment in any industry; benefits are only weakly related to contributions; and the program is burdened with multiple explicit income transfers. The result is, as so many studies note, that Canada spends too much on passive income transfers and not enough on active labor market programs.

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[50] For example, Canada, Royal Commission on the Economic Union and Development Prospects for Canada [Macdonald Commission], *Report* (Ottawa: Supply and Services Canada, 1985); vol. 2, pp. 616–619; Canada, Commission of Inquiry on Unemployment Insurance [Forget Commission], *Report* (Ottawa: Supply and Services Canada, 1986), chap. 11; and Economic Council of Canada, *Good Jobs, Bad Jobs: Employment in the Service Economy* (Ottawa, 1990).

The model to copy in this domain is undoubtedly that of Sweden. Both Sweden and Canada spend 2 to 3 percent of GDP on labor market policies, but whereas three-quarters of Canadian expenditures are for basically passive programs of income transfer, Sweden spends less than one-third on untied transfers.[51] A geographically compact country with only one-third Canada's population, Sweden has decentralized administration of its labor market programs into regional agencies representing government, unions, and business.

After a half century, Canada should experiment with a constitutional reallocation. The federal proposals recommend that labor market training be explicitly transferred to the provinces. I concur, with the qualification that it may be appropriate for the small provinces to delegate their authority, creating, say, a single Atlantic and a single Prairie agency to handle this function.

Ideally, labor training should be integrated with unemployment insurance, and the provinces should simultaneously become constitutionally responsible for this function. Reform of unemployment insurance poses immensely controversial political problems, however. An efficient program would cease to provide permanent subsidies to workers in low-productivity, unstable industries, such as fishery and forestry, which are disproportionately concentrated in Atlantic Canada and particular regions elsewhere in the country. An efficient unemployment insurance and labor training program would generate considerable migration out of these regions. In the long run, the departure of these workers would substantially reduce the net transfer of income to the Atlantic region, which, in turn, would induce further outmigration.

Ottawa could, in principle, continue financing unemployment insurance and labor training, engaging in block transfers — as with health and education funding — to provincially controlled agencies responsible for these services. Thereby, we would retain the advantages of financing from the more stable national revenue base, while block transfers forced regional interest groups to face a budget constraint and internalize the costs of overfunding passive income support and underfunding retraining and mobility. Although it is possible to conceive such a reform in principle, it is unlikely that federal politicians would be willing to bear the political cost of raising the tax revenue for what is the most costly single federal program, transfer the funds to provincially controlled agencies, and exercise no control over the resulting programs.

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[51] Economic Council of Canada, *Good Jobs, Bad Jobs*, p. 21.

In summary, we should not expect to resolve the conundrum of unemployment insurance in this constitutional round. It would be enough to make interprovincial competition to improve labor training constitutionally feasible.

Recommendation 9: Provision for the Constitutional Equality of the Two Orders of Government

> *The* Constitution Act *should be amended to embody a statement to the effect that a fundamental characteristic of Canada is its federal form of government and that the two orders of government are responsible and accountable within their respective jurisdictions. Other amendments should delete the numerous provisions that imply, incorrectly, that Canada is only a quasi-federation, as opposed to the genuine federation into which it evolved during the first half-century after Confederation.*

Canada owes much of its success as a country to the creativity with which it has applied the federal principle. The Canada clause of the federal proposals appropriately starts off with the statement that Canada is "a federation whose identity encompasses the characteristics of each province, territory and community."[52] The Beaudoin-Dobbie Committee's proposed Canada clause begins in a like manner: "We, Canadians all, convinced of the nobility of our collective experiment, hereby renew our historic resolve to live together in a federal state."[53] Although the division of powers can never be entirely watertight — some functions must be jointly managed — I believe that undertaking Jefferson's "division and subdivision of duties" is a worthy exercise. There are some reforms, many of which the federal proposals address, that would constitutionally acknowledge our commitment to a federal future.

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[52] The federal proposals, section 7.

[53] The Beaudoin-Dobbie report, p. 106.

The Group of 22 summarized the case for such reforms:

> We have concluded that the constitutional equality of the two orders of government should be more fully expressed and accepted. Given the maturity of our federal system, Ottawa need not continue to protect provinces and provincial populations from themselves. This implies, however, that Canadians should stop running to Ottawa to fix the alleged misdeeds of their provincial government. The democratic process exists in the provinces to permit provincial residents to correct perceived provincial wrongs. It implies, as well, that provincial governments should restrain themselves from intervening in areas of federal jurisdiction.[54]

Specifically, I recommend the following:

- I concur with the federal proposal on the residual power, which currently lies with Ottawa (preamble to section 91 and section 91(29)). There should be no presumption that the appropriate jurisdiction for unallocated functions lies with one or the other level of government. Allocation should depend on the merits of the case.
- Ottawa currently has the power to declare public works, otherwise within provincial jurisdiction, to be for the "general advantage of Canada" and henceforth subject to federal jurisdiction (section 92(10)(c)). This power should be abolished, as the federal proposals suggest.
- Ottawa has the constitutional powers to disallow provincial legislation and to instruct a lieutenant-governor to reserve

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[54] Group of 22, *Some Practical Suggestions for Canada* (Montreal: Le Groupe Columbia Inc., 1991).

Royal Assent (sections 56, 57, and 90). These powers have fallen into disuse, and they should be abolished.

- Ottawa currently nominates lieutenant-governors to each province. The *Constitution Act* (section 58) should be amended so that each province can designate, by election or appointment, its own symbolic representative of the Crown.
- The federal spending power should be specifically constrained. The power of the federal government to spend revenue in any way it wishes, regardless of division of jurisdiction, is not explicitly sanctioned by the *Constitution Act*, but it has become an accepted constitutional practice.

An unconstrained federal spending power is simply incompatible with a federal state. It encourages interest groups intent on particular spending programs to lobby both levels of government, and destroys the benefits from a stable constitutional division of powers. In principle, neither level of government should have the power to spend in the jurisdiction of the other, except by mutual agreement. Given the vast number of existing federal-provincial shared-cost programs, complete disentanglement would be both cumbersome and undesirable. But I agree with the traditional Quebec position: The Constitution should specify that if Ottawa launches any future program in an area of provincial jurisdiction, a province may opt out and receive financial compensation reasonably equivalent to the cost of the forgone benefits.

Constraining the federal government's spending power is controversial. Many defend that power as essential for the extension of the welfare state into new domains, such as child care. The battle between defenders and critics has centered on specifying constraints on compensation payable to provinces that choose to opt out. The Meech Lake Accord would have permitted compensation "if the province carrie[d] on a program or initiative that is compatible with the national objectives" (section 106A). The federal government's proposals and the Beaudoin-Dobbie Committee would permit compensation on the slightly narrower grounds of a province's carrying on programs "meeting the objectives of the new Canada-wide program."[55] Ardent defenders of the federal spending power want compensation only if the alternative provincial program satisfies national standards. This position is in effect a critique of the federal principle and should be recognized as such. If we are to continue to enjoy the benefits of intergovernmental competition in the design of government programs, there should be few constraints on compensation.

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[55] The federal proposals, section 27.

Appendix: The Federal Constitutional Proposals, September 1991

Part I: Shared Citizenship and Diversity

1. Reaffirming the rights and freedoms of citizens. The Government of Canada reaffirms the basic rights set out in the Charter as a fundamental feature of the Canadian Constitution. The Government of Canada proposes that the *Canadian Charter of Rights and Freedoms* be amended to guarantee property rights. The Government of Canada further proposes that the votes necessary for Parliament or a provincial legislature to invoke the override (section 33) be changed from a simple majority to 60 percent of the members of Parliament or the provincial legislature.

2. Recognition of Quebec's distinctiveness and Canada's linguistic duality. The Government of Canada proposes that a section be included in the Charter stating that the Charter of Rights and Freedoms shall be interpreted in a manner consistent with the recognition of Quebec as a distinct society within Canada. The section would read:

25.1 (1) This Charter shall be interpreted in a manner consistent with

(a) the preservation and promotion of Quebec as a distinct society within Canada; and

(b) the preservation of the existence of French-speaking Canadians, primarily located in Quebec but also present throughout Canada, and English-speaking Canadians, primarily located outside Quebec but also present in Quebec.

(2) For the purposes of subsection (1), "distinct society", in relation to Quebec, includes

(a) a French-speaking majority;
(b) a unique culture; and
(c) a civil law tradition.

3. Aboriginal participation in current constitutional deliberations. The Government of Canada is committed to ensuring that aboriginal peoples participate in the current constitutional deliberations.

4. *Aboriginal self-government*. The Government of Canada proposes an amendment to the Constitution to entrench a general justiciable right to aboriginal self-government within the Canadian federation and subject to the *Canadian Charter of Rights and Freedoms*, with the nature of the right to self-government described so as to facilitate interpretation of that right by the courts. In order to allow an opportunity for the Government of Canada, the governments of the provinces and the territories, and aboriginal peoples to come to a common understanding of the content of this right, its enforceability would be delayed for a period of up to 10 years. The Special Joint Committee should examine the broad parameters of the right to be entrenched in the Constitution and the jurisdictions that aboriginal governments would exercise.

5. *Aboriginal constitutional process*. The Government of Canada proposes the entrenchment of a constitutional process to address aboriginal matters that are not dealt with in the current constitutional deliberations and to monitor progress made in the negotiations of self-government agreements.

6. *Representation of aboriginal peoples in the Senate*. The Government of Canada proposes that aboriginal representation should be guaranteed in a reformed Senate.

7. *A Canada clause in the Constitution*. The Government of Canada proposes that a "Canada clause" that acknowledges who we are as a people, and who we aspire to be, be entrenched in section 2 of the *Constitution Act, 1867*. The Government of Canada believes that it would be appropriate for the following characteristics and values to be reflected in such a statement:

- a federation whose identity encompasses the characteristics of each province, territory and community;
- the equality of women and men;
- a commitment to fairness, openness and full participation in Canada's citizenship by all people without regard to race, colour, creed, physical or mental disability, or cultural background;

- recognition that the aboriginal peoples were historically self-governing, and recognition of their rights within Canada;
- recognition of the responsibility of governments to preserve Canada's two linguistic majorities and minorities;
- the special responsibility borne by Quebec to preserve and promote its distinct society;
- the contribution to the building of a strong Canada of peoples from many cultures and lands;
- the importance of tolerance for individuals, groups and communities;
- a commitment to the objective of sustainable development in recognition of the importance of the land, the air and the water and our responsibility to preserve and protect the environment for future generations;
- respect for the rights of its citizens and constituent communities as set forth in the *Canadian Charter of Rights and Freedoms*;
- the free flow of people, goods, services and capital throughout the Canadian economic union and the principle of equality of opportunity throughout Canada;
- a commitment to the well-being of all Canadians;
- a commitment to a democratic parliamentary system of government;
- the balance that is especially Canadian between personal and collective freedom on the one hand and, on the other hand, the personal and collective responsibility that we all share with each other.

Part II: Responsive Institutions for a Modern Canada

8. House of Commons. The Government of Canada commits itself to a process of further parliamentary reform to given individual MPs more free votes and to reduce the application of votes of confidence.

9. Principles of Senate reform: an elected, effective and more equitable Senate. the Government of Canada proposes that:

- the Senate be directly elected;
- Senate elections coincide with elections to the House of Commons;
- the Senate's composition provide for much more equitable provincial and territorial representation than at present;
- the House of Commons remain the primary legislative body;
- as a general rule, in order for measures to become law, approval of both the Senate and the House of Commons should be required as at present;
- for matters of language and culture, the Senate would also have a double majority special voting rule;
- for matters of national importance, such as national defence and international issues, the Senate would have a six-month suspensive veto. Following expiry of the suspensive veto, the House of Commons would be required to repass the legislation for it to become law;
- since the Senate is not a confidence chamber, the Senate would have no legislative role in relation to appropriation bills and measures to raise funds including borrowing authorities;
- guaranteed representation be provided for aboriginal Canadians in the Senate;
- the Senate continue to have a mandate to conduct special inquiries into issues of public policy.

10. Details of Senate reform. The Government of Canada proposes that the Special Joint Committee of Parliament consider the following issues:

- the form of direct election to the Senate;
- the appropriate number and distribution of Senate seats;
- in consultation with the aboriginal peoples, the appropriate representation of Canada's First Peoples.

11. Senate Ratification of Appointments to Regulatory Boards and Agencies. The Government of Canada proposes that the Senate be given a mandate to ratify the appointment of the Governor of the

Bank of Canada and the appointments of the heads of national cultural institutions, such as the Canadian Broadcasting Corporation, the National Film Board, the National Library, the National Archives, the national museums, the Canadian Film Development Corporation, the Canada Council and the National Arts Centre, as well as the heads of regulatory boards and agencies such as the National Energy Board, the National Transportation Agency, the Canadian Radio-television and Telecommunications Commission, the Immigration and Refugee Board, and the proposed Canadian Environmental Assessment Agency.

12. Appointments to the Supreme Court of Canada. The Government of Canada will introduce a constitutional amendment to provide for a role for the provinces and the territories in Supreme Court appointments whereby appointments would be made by the federal government from lists of nominees submitted by provincial and territorial governments, the individual appointed being acceptable to the Queen's Privy Council of Canada.

In addition, the Government of Canada would be prepared to proceed with the entrenchment in the Constitution of the Supreme Court and its composition if it were found desirable to proceed with any unanimity items in the final package.

13. The Constitutional Amending Formula. The Government of Canada would be prepared to proceed with changes to the amending formula as specified in the Meech Lake Accord if a consensus on this matter were to develop; if the accession of existing territories to provincehood were to proceed on the basis of the current amending formula; and if it were found desirable to proceed ultimately with any items requiring unanimous consent in the final package.

Part III: Preparing for a More Prosperous Future

14. Broadening s. 121, the common market clause. The Government of Canada proposes that section 121 of the *Constitution Act, 1867* be amended to read as follows:

121. (1) Canada is an economic union within which persons, goods, services and capital may move freely without barriers or restrictions based on provincial or territorial boundaries.

(2) Neither the Parliament or Government of Canada nor the legislatures or governments of the provinces shall by law or practice contravene the principle expressed in subsection (1).

(3) Subsection (2) does not render invalid

(a) a law of the Parliament of Canada enacted to further the principles of equalization or regional development;

(b) a law of a provincial legislature enacted in relation to the reduction of economic disparities between regions wholly within a province that does not create barriers or restrictions that are more onerous in relation to persons, goods, services or capital from outside the province than it does in relation to persons, goods, services or capital from a region within the province; or

(c) a law of the Parliament of Canada or of the legislature of a province that has been declared by Parliament to be in the national interest.

(4) A declaration referred to in paragraph (3) (c) shall have no effect unless it is approved by the governments of at least two-thirds of the provinces that have, in the aggregate, according to the then latest general census, at least 50 percent of the population of all the provinces.

(5) This section shall come into force on July 1, 1995.

15. Power to Manage the Economic Union. The Government of Canada proposes that the following section be added to the *Constitution Act, 1867* immediately after section 91:

91A. (1) Without altering any other authority of the Parliament of Canada to make laws, the Parliament of Canada may exclusively make laws in relation to any matter that it declares to be for the efficient functioning of the economic union.

(2) An Act of the Parliament of Canada made under this section shall have no effect unless it is approved by the governments of at least two thirds of the provinces that have, in the aggregate, according to the then latest general census, at least 50 percent of the population of all the provinces.

(3) The legislative assembly of any province that is not among the provinces that have approved an Act of the Parliament of Canada under subsection (2) may expressly declare by resolution supported by 60 percent of its members that the Act of Parliament does not apply in the province.

(4) A declaration made under subsection (3) shall cease to have effect three years after it is made or on such earlier date as may be specified in the declaration.

The Government of Canada also proposes that the Special Joint Committee consider whether the opting-out provision should be renewable.

16. *Harmonization of economic policies.* The Government of Canada proposes to develop, with the provinces, an annual timetable to allow for more open and visible budget-making processes.

The Government of Canada proposes to develop, with the provinces, guidelines to improve the coordination of fiscal policies and the harmonization of fiscal policies with Canada's monetary policy. Once approved, these guidelines would be set in federal legislation under the new economic union power. Accordingly, these guidelines would require the approval of at least seven of the provinces representing 50 percent of the population, and up to three provinces could opt out.

The Government also proposes to discuss with the provinces the establishment of an independent agency to monitor and evaluate the macroeconomic policies of the federal and provincial governments.

17. *Reforms to the Bank of Canada.* The Government of Canada proposes to amend the *Bank of Canada Act* to make it clear that the mandate of the Bank is to achieve and preserve price stability. To ensure regional representation on the Board of Directors of the Bank of Canada, the Government will solicit the views of provincial and territorial governments and consult with them before making appointments to the Board. In addition, the Government proposes to create regional consultative panels to advise the Directors of the Bank on regional economic conditions. The Government will also solicit the views of provincial and territorial governments with

respect to the membership of the regional panels. Moreover, the appointment of the Governor of the Bank of Canada would be subject to Senate ratification.

18. Training. The Government of Canada proposes that section 92 of the *Constitution Act, 1867* be amended to recognize explicitly that labour market training is an area of exclusive provincial jurisdiction.

19. Immigration. While recognizing the federal role in setting Canadian policy and national objectives with respect to immigration, the Government of Canada is prepared to negotiate with any province agreements appropriate to the circumstances of that province and to constitutionalize those agreements.

20. Culture. The Government of Canada will negotiate with the provinces, upon their request, agreements appropriate to the particular circumstances of each province to define clearly the role of each level of government. Where appropriate, such agreements would be constitutionalized.

21. Broadcasting. The Government of Canada proposes to:

1. consult with the provinces on the issuance of new licences;

2. provide provincial governments and their agents with the opportunity to evolve into full public broadcasting undertakings with varied programming, subject to CRTC regulation;

3. further regionalize the operations of the CRTC and expand the roles of its regional offices;

4. allow for provincial participation in the nomination of regional commissioners of the CRTC.

22. The Residual Power. The Government of Canada proposes to reserve to itself the Peace, Order and Good Government clause of the *Constitution Act, 1867* to maintain its authority to deal with national matters or emergencies. However, the Government of Canada is prepared to transfer to the provinces authority for non-national matters not specifically assigned to the federal government under the Constitution or by virtue of court decisions.

23. The Federal Declaratory Power. The Government of Canada is prepared to support a constitutional amendment to remove to declaratory power set out in section 92(10)(c).

24. Recognizing Areas of Provincial Jurisdiction. Within this framework, the Government of Canada is committed to ensuring the preservation of Canada's existing research and development capacity obligations for international and native affairs. The Government of Canada is prepared to recognize the exclusive jurisdiction of the provinces and discuss how best to exercise its own responsibilities in a manner appropriate to the sector in the following areas:

- tourism
- forestry
- mining
- recreation
- housing
- municipal/urban affairs.

25. Legislative Delegation. The Government of Canada endorses the recommendation of the Beaudoin-Edwards Joint Parliamentary Committee that there be a constitutional amendment providing for delegation of legislative powers between Parliament and the legislatures, and that there be provisions inserted in the Constitution to enable the delegation of legislative authority between the two levels of government with the mutual consent of the legislative bodies involved.

26. Candidates for Streamlining. In order to provide Canadians with the best service at the lowest possible cost, the federal government is prepared to discuss with the provinces the rationalization of government is prepared to discuss with the provinces the rationalization of government programs and services by reviewing which level of government can best deliver them. All proposals from the provinces will be considered. As a starting point, the Government proposes to discuss the following areas with the provinces:

- drug prosecutions

- wildlife conservation and protection
- transportation of dangerous goods
- soil and water conservation
- ferry services
- small craft harbours
- some aspects of financial sector regulation
- some aspects of bankruptcy law
- some aspects of unfair trade practices
- inspection programs.

27. The Exercise of the Federal Spending Power in Areas of Exclusive Provincial Jurisdiction. The Government of Canada commits itself not to introduce new Canada-wide shared-cost programs and conditional transfers in areas of exclusive provincial jurisdiction without the approval of at least seven provinces representing 50 percent of the population. This undertaking would be entrenched in the Constitution. The constitutional amendment would also provide for reasonable compensation to non-participating provinces which establish their own programs meeting the objectives of the new Canada-wide program.

28. Working Together: A Council of the Federation. The Government of Canada proposes the entrenchment of a Council of the Federation, composed of federal, provincial and territorial governments, that would meet to decide on issues of intergovernmental coordination and collaboration. The Council would have the mandate to vote on proposed federal legislation to enhance the functioning of the economic union under the proposed new head of power; to vote on guidelines for fiscal harmonization and coordination as well as to decide on processes to improve future collaboration in this area; and to make decisions on the use of the federal spending power on new Canada-wide shared-cost programs and conditional transfers in areas of exclusive provincial jurisdiction. All decisions of the Council of the Federation would require the approval of the federal government and of at least seven provinces representing 50 percent of the population.

Social Security and the Division of Powers in Canada

Jean-Michel Cousineau

Introduction

Canada is now experiencing a crisis of economic, political, and social dimensions, a crisis that turns on the issue of the division of powers. Canadians are asking what powers the provinces, the regions, and the federal government should enjoy with respect to language, culture, communications, social security, and the economy in general. The economic aspects of this problem often attract the attention of both the politicians and the general public. In the current economic literature, there are several theoretical models to help us examine this issue, but their outcome for the Canadian situation remains to be defined and they need to be discussed more or less independently of various responsibility.[1] This essay constitutes a consideration of one particular field of specific responsibility: social security.

I gratefully acknowledge the comments and suggestions of Gilles Beausoleil, Jac-André Boulet, André Blais, Claude d'Aoust, Margaret Hoogeveen, Irene Ip, John McCallum, Normand Poulet, André Raynauld, Daniel Schwanen, and François Vaillancourt. However, the opinions expressed in this text are mine alone, and I take full responsibility for them. I am very grateful to the C.D. Howe Institute for translating and publishing this paper.

[1] For a general discussion of the division of powers in a federal state, see Gérard Bélanger, "The Division of Powers in a Federal System: A Review of the Economic Literature, with Apllications to Canada," in R. Simeon, research coordinator, *Division of Powers and Public Policy*, Collected Research Studies of the Royal Commission on the Economic Union and Development Prospects for Canada 61 (Toronto: University of Toronto Press, 1985), pp. 1–29.

Social security consumes large sums of money in Canada, as it does in most industrialized countries. In 1989, for example, the total amount spent on family allowance, old age security, guaranteed income supplements and spousal grants for the elderly, the Canada Pension Plan, the Quebec Pension Plan, welfare, unemployment insurance, federal manpower programs, and health insurance was $83.3 billion. That means Canada spends more than one out of every ten dollars of its annual gross domestic product (GDP) on social security.[2] As a result, social security and the income redistribution associated with it constitute one of the largest industries in Canada. This "industry" involves various levels of government through their various programs and departments, which, to a certain extent, compete with each other. As is the case in any industry, adequate resources are required, and these resources should be distributed as efficiently and effectively as possible throughout Canada — that is, so that they help further the interest and maximize the well-being of all members of Canadian society.

The methodology used in this essay consists essentially of recalling some basic theoretical frameworks and applying to them the various empirical aspects of the Canadian situation, to determine a division of powers that would be most efficient for Canada. The essay begins with an analysis of the redistribution of income, and returns later to the general question of social security as a whole.

The Redistribution of Income and the Centralization of Powers

Traditionally, the economic analysis of income redistribution approaches its subject from the perspective of altruism. Economists generally make a fundamental assumption that the well-being of nonpoor individuals, or those in the middle- and upper-income brackets, is directly and positively related to the well-being of poor individuals. In other words, when the well-being of the poor increases, so does the well-being of the nonpoor.[3]

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[2] The data sources are: Canada, Department of National Health and Welfare, *Précis sur les programmes de sécurité sociale, juillet 1989* (Ottawa: Supply and Services Canada, 1990); and Canada, Department of Finance, *Quarterly Economic Review*, June 1991. For welfare and health insurance spending, I have doubled the level of expenditure declared by the federal government. As indicated in footnote 22, this operation underestimates total expenditures for all governments in the field of health insurance.

According to this assumption, nonpoor individuals have an interest in, and derive satisfaction from, transfers of income to poor persons, and what we call charity can thus be defined as an activity that responds to perceived needs, but that also increases the general well-being. Things become more complicated, however, when such charity or transfer payments are strictly a matter of private initiative. In such circumstances, the existence of important externalities is overlooked. For instance, a person who helps another primarily increases the well-being of the person helped, but also increases his or her own well-being. In addition, all the other people who have not given help also derive benefits from this action. A gap is thus created between the social benefits (experienced by society as a whole) and the private benefits (experienced by donors and persons assisted). The state must intervene to close this gap, to see that everyone pays for the benefits they derive and thereby ensure a better distribution of income. According to this approach, income redistribution, or at least a large part of it, should be entrusted entirely to and assumed by the highest level of government — that is, the central government. Two kinds of reasons are usually given.

First, if income redistribution were left to operate on the local or regional level, some jurisdictions might give a higher priority to redistributing income to poor people than others do. This would result in generous support being given to poor people in these jurisdictions, but also higher taxes for the nonpoor in the given tax base. The immediate consequences of such differences in the levels of both payments and taxes would be a move of poor people to the more generous regions,[4] accompanied by an exodus of taxed persons in the opposite direction, to the less generous regions. This situation would be counterproductive for obvious reasons.

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[3] For a general discussion of income redistribution, see R.W. Boadway and D.E. Wildasin, *Public Sector Economics* (Toronto: Little, Brown and Company, 1984), pp. 445–543.

[4] On condition, of course, that the eligibility rules allow it.

On the other hand, the regions wanting to be more generous could be well aware of the risks involved, and consequently might make lower payments than they had wanted, resulting in a less-than-satisfactory redistribution to the poor. Finally, if some regions did manage to maintain slightly higher levels of grants than others, it could result in both counterproductive population shifts *and* unsatisfactory redistribution.[5]

The second argument in favor of centralizing the redistributive function of governments is based on the work of J.M. Buchanan.[6] According to this approach, even if income in all provinces were taxed equally — that is, in exactly the same proportion — the tax surpluses would vary from province to province because each has a different tax base. On the one hand, individuals earning $30,000 in a rich province would pay $6,000 in tax — assuming a tax rate of 20 percent — but would benefit from public spending of, say, more than $4,500.[7] They would lose the benefit of less than $1,500. On the other hand, in poor provinces, individuals with the same earnings would still pay taxes amounting to $6,000 but would only benefit from public spending of less than $3,500 on public goods.[8] This situation would result from the narrower tax base in the poorer provinces. These people would each lose the benefit of more than $2,500. So, despite all citizens paying the same amount of tax for their income level, some parties would still benefit more than others. As a result, it would be in the interest of richer individuals to move to richer states.

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[5] See G.J. Stigler, "Tenable Range of Functions of Local Government," in *Federal Expenditure Policy for Economic Growth and Stability*, United States, Congress, Joint Economic Committee, Subcommittee on Fiscal Policy (November 5, 1957): 213–219; R.A. Musgrave, *The Theory of Public Finance* (New York: McGraw-Hill, 1959); and W.E. Oates, *Fiscal Federalism* (New York: Harcourt Brace Jovanovich, 1972).

[6] J.M. Buchanan, "Federalism and Fiscal Equity," *American Economic Review* 40 (1950): 583–599.

[7] In Boadway and Wildasin (*Public Sector Economics*, pp. 445–543), the amount is $4,667.

[8] $3,333 in the example given in ibid.

A perfectly symmetrical argument can be made for the situation of poorer people as well. The poorest individuals — those with, say, $10,000 income per year — would pay only $2,000 in taxes in whatever province they lived, but the per capita public expenditure in a rich province would clearly be higher than that in a poor province. The monies spent would exceed the $2,000 paid by the poorer individual in both provinces but would be higher in the rich province than in the poor province.[9] In these cases, and contrary to the previous analysis, *both* the poor and the rich would tend to migrate to the richest regions and leave the poorest ones.

Whatever approach is adopted, the conclusion is the same: Decentralizing the power to redistribute wealth from the nonpoor to the poor cannot help but be inefficient. There are, in fact, several more complex models that allow a degree of decentralization,[10] but they assume explicitly that all taxpayers and all beneficiaries of transfer payments would never undertake to move, no matter what the level of taxes and transfers. In sum, if only the above aspects are considered, the problem could easily be resolved. This analysis, however, considers only one part of social security and assumes there is no cost to centralization and, indeed, no alternatives. In the following paragraphs, I will explore these possibilities.

Social Security, Income Redistribution, and the Decentralization of Powers

Income redistribution activities, it is important to point out, are not motivated only by altruism. A large portion of them — indeed, even the majority — involve collective social insurance programs. That is the case, for example, of health insurance, the Canada and Quebec

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[9] By $2,667 in the first case and $1,333 in the second, according to the example in ibid.

[10] See M.V. Pauly, "Income Redistribution as a Local Public Good," *Journal of Public Economics* 2 (1973): 35–58.

Pension Plans, disability pensions, unemployment insurance, and compensation paid for industrial accidents (including occupational diseases). In fact, there are only two redistributive programs aimed directly at eliminating poverty: guaranteed minimum income security and the spousal allowance for the elderly, on the one hand, and the Public Assistance Plan of Canada (welfare) on the other.

These two programs account for spending in the order of only $14.6 billion, whereas the other social security programs mentioned above account for $52.1 billion.[11] The collective insurance programs have been instituted to cover risks and uncertainties linked to income instability: the risk of unemployment in unemployment insurance; the risk of disability in the case of disability pensions; the risk of running out of income after retirement, or of having accumulated too many assets before retirement in the case of the Canada and Quebec Pension Plans; the risk of industrial accidents and occupational diseases in the case of workers compensation; and the risk of illness in the case of health insurance.[12] In relation to these programs, individuals are not being altruistic or thinking of others so much as of themselves and the risks they face. Furthermore, these programs provide protection not against poverty but against instability of income and the standards of consumption to which people have become accustomed. The reason that the state intervenes in these cases cannot be considered as strictly to redistribute wealth from the nonpoor to the poor. Because real or potential private industry, such as the insurance industry, cannot afford to offer the optimal levels of protection against these various kinds of risks, government steps in to offer the citizenry the material and financial advantages to be had in combining risk. Governments thereby transform themselves into distributors of public services, just as they are distributors of public goods such as parks, highways, and public lighting.

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[11] Canada, Department of National Health and Welfare, *Précis sur les programs de sécurité sociale, juillet 1989*.

[12] These programs have redistributive effects between individuals, groups of individuals, and sometimes even regions and sectors. In the case of the Atlantic provinces, for example, it is clear that they benefit from substantial transfers for unemployment insurance. For a review of the main social security programs in Canada see ibid.; and F. Vaillancourt, "Income Distribution and Economic Security in Canada: An Overview," in F. Vaillancourt, research coordinator, *Income Distribution and Economic Security in Canada*, Collected Research Studies of the Royal Commission on the Economic Union and Development Prospects for Canada 1 (Toronto: University of Toronto Press, 1985), pp. 1–86.

At this point, the analysis moves in a very different direction. If social security programs are evaluated as though they are public services, which have the additional feature of interacting with regional economic development — as does unemployment insurance, welfare, and vocational training — Oates's theorem[13] can be applied very effectively. Following Oates's approach, one is led to consider that there may be differences in collective or social preferences, especially in regard to the needs associated with variable economic conditions. Accordingly, differing demands for such public services will arise in any given pair of regions. In these circumstances, if we also assume that the marginal costs of producing these public goods are identical for the two regions, there will be two quantities of public goods (G_1 and G_2 on Figure 1) produced for each of the regions (R_1 and R_2), which will, in turn, maximize the well-being in each of the regions and the collective well-being of Canada as a whole.

In this context, any intervention by a third level of government can only reduce the level of utility or well-being of either of the regions or both at once. Various assumptions were necessary to reach this conclusion, as follows:

- the similarity of marginal, or minimum, costs of production,
- the equalization of interregional fiscal deficits and surpluses, and
- the absence of externalities.

In the following sections, we will examine the implications of these three assumptions for the division of powers.

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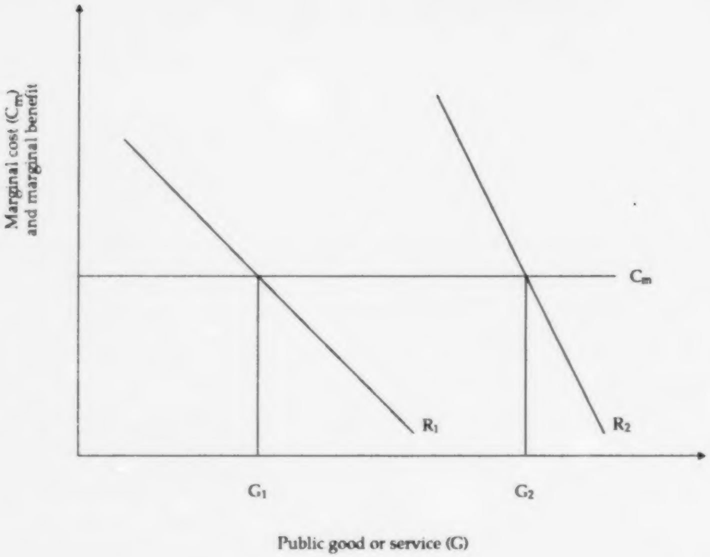
[13] Oates, *Fiscal Federalism*.

Figure 1: *Decentralization and the Social Optimum*



The Similarity of Marginal Costs of Production

To analyze whether marginal costs of production are on a par involves, in fact, two distinct problems. On the one hand, it is necessary that the costs in a decentralized form of management be analogous or even less than those in a centralized one.[14] On the other hand, costs must also be as similar as possible from region to region.

With respect to the first problem, there are several reasons why the decentralization of social security programs — including the most "redistributive" of programs, such as welfare — is likely to be less expensive and more efficient, while only one reason speaks to the advantage of centralization.

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[14] This aspect can be related as well to the costs of organization characterizing each of the different levels of government. See A. Breton and A. Scott, *The Economic Constitution of Federal States* (Toronto: University of Toronto Press, 1978); and idem, *The Design of Federations* (Montreal: Institute for Research on Public Policy, 1980).

First of all, it appears that the problems to be solved and the types of risks to be assumed vary substantially from region to region. The seasonal nature of the fisheries in Newfoundland is a problem that is clearly different from the problem of job instability in Toronto. If the problems are different, obviously the solutions must be different as well. And if the solutions are variable, it is both likely and desirable that the nature and combination of the tools used in the solutions — that is, unemployment insurance, welfare, and vocational training — will also be very different. For optimum efficiency, these programs must be flexible. To impose uniform federal standards would only be expensive and inefficient.

Second, the amount of information to be processed can prove to be very large — for welfare and vocational training in particular — because they involve case-by-case handling for beneficiaries and often companies as well.

Third, the costs of adjustments, or manpower mobility, are greatly reduced at the provincial or regional level, mainly because the homogeneity of general training (education systems), specific training, technology, and physical "capital" (regional concentrations and industrial specializations) reduces transaction costs.

Fourth, in a known universe solutions would be technical and apparent, and there would be no need for the expression of preferences with respect to the means used for solving problems. But we live in an uncertain universe, and, just like individuals, each region has its own measures and preferences peculiar to itself. The regions may want to experiment with solutions, take initiatives, and innovate. We have already compared social security to a major industry, and like any industry, it needs innovation for dynamic efficiency. The decentralization formula is the one best suited for the development of innovation.

A fifth point with regard to costs works in favor of centralization: the size of the jurisdiction. Whether to achieve significant economies of scale with respect to the management of pension funds or to absorb relatively brutal shocks from unemployment, a large population is required if one wants to offer competitive services. Unit costs, in the first case at least, are an asymptotic function; up to a certain point the larger the community, the lower the unit costs. These factors led me to define decentralization in terms of the five major regions of Canada: the Atlantic provinces (2.3 million inhabitants); Quebec (6.8 million); Ontario (9.7 million); the Prairie provinces (4.6 million); and British Columbia (3.1 million).[15]

These five major regions would offer the advantage of costs of production that are economically feasible, given the size of the populations involved, as well as being quite similar.

The Equalization of Fiscal Surpluses and Deficits

In Figure 1, it is explicitly assumed that fiscal surpluses and deficits are perfectly balanced. Initially, however, there are major differences between the provinces in terms of their tax bases. At the present time, Ottawa partially resolves this problem through transfer payments to the various provinces.[16] Clearly, the major regions would be no more able than the provinces to assume the required transfer payments privately and independently of each other. This is another important deficiency associated with the decentralization of powers, but one for which there is again an alternative solution that applies to purely redistributive programs, as such, as well as to the collective insurance programs: the central government would act as main intervener in balancing the surpluses and deficits. Boadway and Flatters[17] clearly specify that an action of this sort reduces the potential for distortions caused by different tax bases.[18]

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[15] This is 1990 data from Canada, Department of Finance, *Economic Review* (June 1991).

[16] A. Raynauld, "The Canadian Federation," *Canadian Journal of Economics* 17 (1984): 635–653.

[17] R.W. Boadway and F.R. Flatters, "Efficiency and Equalization Payments in a Federal System of Government: A Synthesis and Extension of Recent Results," *Canadian Journal of Economics* 15 (1982): 613–633.

The Externalities

The problem of externalities can crop up in a number of ways; I will concentrate on one: When the positive spinoffs that actions by one region have on other regions are not accounted for in the calculations, strategies, and policies of either the contributor or recipient regions. I will consider, more specifically, vocational training. If one region undertakes training activities, and a portion of the people so trained find work in another region, this would constitute a form of external influence for which the training region is not compensated. Although most such externalities are intraregional rather than interregional,[19] it would severely limit the benefits of decentralization if regions were not to account for interregional externalities, as should be done. A clear-cut and efficient solution to this problem would be to institute a federal compensation board for dealing with any externalities. Such an institution would oversee zero-sum federal transfers conditional on interregional migratory imbalances that could be explicitly integrated in the general transfer payment formulas.[20]

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[18] We have consciously excluded the concepts of vertical and horizontal equity from the analysis in order to concentrate on efficiency. Briefly, however, it is possible to consider that (a) equalization payments offer a form of vertical equity while being effective and (b) that the concept of horizontal equity (uniform standards) is a subsidiary concept to efficiency. That is to say, once the appropriate level of jurisdiction has been identified in terms of efficiency, it is then appropriate to apply the concept of equality of treatment and of standards for all those who fall under this jurisdiction. This does not exclude, however, that co-opted minimum uniform standards be established, as will be discussed in the next section.

[19] J.R. Baldwin and P.K. Gorecki, *Structural Change and the Adjustment Process: Perspectives on Firm Growth and Worker Turnover* (Ottawa: Economic Council of Canada, 1990).

[20] As for what data the operation of the Federal Compensation Board would use as its basis, the detailed data from the five-year censuses might be appropriate. But more timely, specific, or regular surveys might be necessary or complementary.

In terms of negative externalities, it is conceivable that one or more regions, on occasion and in certain circumstances, might create artificial barriers to prevent manpower from arriving or leaving. This could take the form, for example, of the nontransferability of funds related to social security or limitations on access to certain fields or projects. To offset these problems, federal councils could be formed, under the initiative of the federal government, to oversee, through co-opting, the standardization of professional codes, the transferability of funds, and the establishment of uniform minimum standards in accordance with the model presented in Figure 1.[21]

The Proposed Solution

The reasoning presented above leads to a simple solution. Grant all of the basic taxation, design, preparation, and implementation powers for social security policies to the five major regions of Canada (as outlined previously), and reserve for the federal government responsibility for the formation of federal councils, conditional transfer payments associated with interregional external influences, and unconditional transfer payments linked to the standardization of regional tax surpluses and deficits. The federal government would, of course, maintain corresponding taxation powers.

A question arises quite naturally at this point: If this solution seems so obvious, why has it not spontaneously developed within the current political system? Presently, family allowances are under federal jurisdiction but the provinces have the right to pay different amounts according to their own scales (Alberta and Quebec do so). Old age security, the guaranteed income supplement, and spousal allowances for the elderly (from ages 60 to 65), are all federal programs. The Canada Pension Plan and the Quebec Pension Plan are Canadian and Quebec jurisdictions, respectively. Unemployment insurance is strictly federal. Compensation for injured workers, including occupational diseases, is provincial. Welfare and health insurance are also provincial, but in keeping with the relevant legislation and regulations, the federal government finances a significant portion of the eligible expenditure made by the provinces.[22] Finally, job placement and vocational training are under shared jurisdiction.

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[21] For a more elaborate discussion of the structure of institutions that would fulfill the purpose of harmonization of regional policies, see J.-M. Cousineau, "Délégations de pouvoirs et mécanismes d'harmonisation et de coordination des programmes et des politiques de main-d'oeuvre au Canada" (École de relations industrielles et Centre de recherche et développement en économique, Université de Montréal, Montreal, April 1992, Mimeographed).

Four reasons can be used to explain why the Canadian political system has not spontaneously generated a structure that appears to be superior to the current one.

First, to escape taxes people may change provinces but will not likely change countries, so the federal government's capacity to tax is substantially greater than that of any of the provinces individually. This confers an obvious advantage to the federal level in terms of its ability to finance various programs, but nevertheless constitutes a source of imbalance: although the provinces may have jurisdictional power, the federal government has the money.

Second, the federal government has much more extensive borrowing capacity than the provincial governments do. Only the federal government can "borrow" funds from the Bank of Canada and thus issue money to finance its activities. However, this power (over deficits and national debt), like the previous one, cannot be described as a source of efficiency in itself.

Third, the well-known, small-group/large-group theory says that, with respect to public choices, a program has a greater chance of being accepted if it provides a significant benefit to a small group, while its costs are diluted among the largest possible whole. The largest possible whole, of course, is the entire country. But this factor, like those mentioned above, cannot be described as a source of efficiency. On the contrary, this structure can lead to sizable distortions in terms of the efficiency and distribution of resources because it favors the allocation of resources to well-organized groups and not necessarily to those whose needs are of the highest priority.

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[22] Before 1977, this portion was 50 percent for both programs. Since 1977, the federal contributions to the health insurance program have depended on demographic variables and the rate of growth of GDP, both of which lowered this percentage. *1988 Canada Yearbook* (Ottawa: Supply and Services Canada, 1987), pp. 3–11.

Fourth, and last, it must be admitted that the present division of powers probably suits the provinces, at least to a certain extent. By entrusting spending and taxation powers to the federal government, the provincial governments free themselves from certain political and social costs they would otherwise have to face. Some present day examples of the transfer or export of social costs include provincial payroll taxes, minimum wage policies, and measures that involve unemployment directly supported by the federal government or all of Canada's workers and employers, as is the case now with the new unemployment insurance program.

All in all, if the current system of division of powers does not correspond to the "ideal" arrangement, there is a very simple reason for it: the imperfection of the political markets. The best solution to such a problem is to include in the Canadian Constitution a clear-cut division of responsibilities, with the least possible overlap. At this time, such a directive does not exist.

Conclusion

This essay began with a brief review of the literature on the division of powers with respect to the redistribution of income. The thesis of centralization offers some strong arguments, posing some difficult problems for the idea of decentralization, but these are not without solutions — for example, equalization payments. But the thesis also contains unsuspected costs in terms of inefficiency.

Seen from a more positive perspective, it appears, on analysis, that Canadians have largely opted for social security programs based on collective and social insurance principles rather than the single principle of vertical redistribution. In this way, they protect themselves against the various risks to which they feel exposed, most of which stem from income instability.

This perspective radically changes the nature of the problem, and takes us toward models and analysis frameworks that are more appropriate. Instead of a division of powers in which the role of the state is to redistribute income in the classic sense of the term, the government becomes more of a vendor of public insurance services that directly interacts in regional economic development.

In such a context, the decentralization of powers appears to be a better solution than centralization. It allows flexibility for various forms of heterogeneity, such as those of preference, community, and economic environment; a closer adjustment of programs to regional constraints; and greater efficiency in the management of various forms of risks and uncertainties. At the same time, by internalizing various costs associated with other forms of provincial intervention, such as the minimum wage and payroll taxes, decentralization makes the various provincial and regional governments more accountable — that is, more responsible for organizing their own economic development to ensure the greater good of all of Canada.[23] In summary, although centralization solves certain problems quite easily, it does not, and cannot, solve all of them; it appears that decentralization would contain benefits that largely outweigh those of centralization, assuming that certain corrective measures were enacted.

Analysis of the decentralization model quickly reveals that it has inherent constraints, including:

- the necessity of forming units of sufficient size to lower costs and make them comparable;
- the management of interregional externalities not assured by such a mechanism; and
- the equalization of fiscal surpluses and deficits.

To offset these various problems or constraints on decentralization, I recommend that:

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[23] This point appears to me to be more important than all the others because it encourages harmonization and consistency of social and economic policies of the regions.

- social security in Canada should be decentralized to five major regions — British Columbia, the Prairie provinces, Ontario, Quebec, and the Atlantic provinces; in this way, social security could respond adequately to the first problem;
- federal subsidies should be employed to compensate the effects of positive externalities generated by the various regions, as cited in the second type of problem; and
- the federal government should grant transfer payments to equalize the tax surpluses and deficits of the various regions, thus resolving the third problem.

If we now ask why the current situation is so different from the proposed system, the answers all appear to be linked in some way to imperfections in the political markets — and none has shown itself to be formally linked to concepts of efficiency. At this point, only one path appears to be likely to correct the situation: inclusion in the Canadian Constitution of a clear-cut division of responsibilities for social security. Based on the objectives, constraints, and methodology used, the solution I propose consists of three segments. First, entrust the five major regions of Canada with all jurisdiction and all taxation powers necessary for the design, preparation, implementation, and application of social security programs. Second, create a federal compensation board and a number of federal councils to manage interregional externalities. And third, keep the transfer power, along with the associated taxation powers, in the hands of the central government.

A Comment on the Allocation of Spending Powers in the Canadian Constitution

Claude E. Forget

Canadian citizens of all stripes have been expressing concern about the future of Canada. Yet remarkably few people have even attempted to describe, in a systematic fashion, their views of an optimal division of powers. Both John Richards and Jean-Michel Cousineau must therefore be commended for the care they have taken to describe many useful ideas for reshaping the allocation of spending powers in Canada. By giving careful explanations of each individual recommendation, they have managed to come up with a comprehensive picture. Indeed, if I were to limit myself to the perspective of these recommendations I might find little to say, because many of them seem plausible and even attractive.

However, I believe it is important to take a step back to get a broader perspective. Therefore, this essay focuses on the general approach Richards and Cousineau have followed, rather than on any of their substantive recommendations.

Richards and Cousineau claim that they have based their recommendations on arguments of "efficiency." These arguments are indicative of a sort of fixation that has been gaining currency in this country for some time: a notion that the concepts of economies of scale, spillover effects, consumer preferences, and the like can help shape an optimal Constitution. In order to be valid, such an approach would require extensive and detailed knowledge about production functions for public goods, voters' preferences, and much else. Little appropriate empirical research has been carried out in Canada that could possibly provide the flesh necessary to cover these conceptual bones. It should be clear that these normative notions of economic efficiency do not constitute explanations of the necessary and inevitable shape of federalism. Whatever the influence of these economic factors, it is obviously insufficient to explain the present organization of the country. Similarly, neither can it be used to forecast the most appropriate organization for the future. Indeed, if there were a "law of efficiency" — analogous to the law of gravity — for political institutions, any discussion of constitutional reform would be an utter waste of time. The search for an efficiency optimum only imperfectly reflects the search for a new political order in Canada, and we must therefore ask ourselves what factors other than those of efficiency are at play.

Constitution Modification: A Response to Policy Failures

I contend that Canadians are attempting to modify the Constitution in an attempt to correct perceived failures of policy. This is also the reason why large organizations, including private business organizations, are restructured. In the latter case, business experts agree that there is not one single optimum form of organization but a large number of equally acceptable structures, all of which depend on factors as diverse as the kind of business being considered, the personalities involved, and the need at any particular time to use restructuring as a means to shift power from one group to another, or to force or facilitate a change in the organizational culture.

In Canada, a sense of policy failure is now widespread. As someone who was deeply involved in the constitutional debate of the late 1970s that led up to the 1980 Quebec referendum, I find it a striking development that reference is now made to a "Canada Round" as opposed to a purely "Quebec Round." In 1980, there was no such thing as a Canadian agenda; there was a federal government agenda, but this was designed to forestall the Quebec government's agenda rather than to redress or correct any fundamental flaw in

Canadian institutions. Since that time, the constituency for change in this country has widened considerably. The West — probably as a result of intense frustration stemming from the imposition of the National Energy Program on Alberta in the 1970s and early 1980s — insists that its views and interests be better represented in Ottawa. Many in Ontario feel threatened by the trend toward globalization, and they feel that the Canada-U.S. Free Trade Agreement is a challenge to Canada's, and particularly Ontario's, identity. The Atlantic provinces feel betrayed by the failure of policies designed to remove disparities. In 1980, it seemed that everyone outside Quebec believed that Canada was basically working well, and they all wanted to persuade Quebecers of that fact. Now it seems that everyone needs convincing.

It is, therefore, hardly surprising that, during the early consultation phase carried out by the joint Senate–House of Commons Committee on the Renewal of Canada, arguments about policy failures overwhelmed debate on the Constitution. It is not irrelevant either that, during the constitutional review, participants in policy debates throughout the country from both the private and public sectors kept referring to the unaddressed challenge of Canada's lack of international competitiveness.

These widely shared frustrations and resentments — the result of long-standing policy failures — are driving the process of constitutional change with much more power than any abstract search for "efficiency." On the one hand, it might be irrational to harp on the poor decisions of Canada's institutions. Indeed, many people have pointed out that to debate the Constitution at a time when Canada has so many unresolved problems of a more immediate and concrete nature is a misplaced emphasis and distraction. And it may well be that changing the Constitution will not help resolve any of those problems. On the other hand, this country does seem to be affected by a paralysis of policy making. The present political institutions seem too overwhelmed by the persistent federal government deficit to be able to tackle it effectively. And nearly 20 years of stagnation in productivity growth — although a serious problem in itself — has perhaps done more harm by undermining Canadians' belief in their ability to emerge from it. Therefore, while it might be a mistake to see a constitutional crisis as a potential solution for bad government, it may present a rich opportunity for changing attitudes. Restructuring is sometimes necessary to change an organization's managerial culture: only a profound shock may suffice to break bad habits.

The search for "optimal" political structures — as defined by Richards and Cousineau — is not radical or powerful enough to trigger a shock. At best, one can only hope that their recommendations will help steer reorganization along acceptable channels. This lack of "shock value" can be attributed to an assumption made by both Richards and Cousineau — one that I feel obliged to challenge. That assumption consists of a notion that an ideal Constitution could somehow result from piecing together a collection of elements, each one of which would be optimal. I do not wish to belittle the importance of searching for and examining the most sensible ways to do things, but, at the end of the day, what matters most is not efficiency in the small but efficiency of the system as a whole including its overall ability to adapt to changing circumstances over time.

On a general level, a parallel can be drawn between the problem of allocation of powers and the resource allocation problem in economics. Unless the initial distribution of wealth is taken as a given, efficiency, in the Pareto sense,[1] has an ambiguous meaning, since there is an infinite number of resource allocation patterns that can be judged to be efficient, each one corresponding to a different distribution of wealth. Similarly, the allocation of "powers," or government jurisdictions, to one level of government or another, can only be termed appropriate or inappropriate by reference to a given degree of centralization—or, in other words, to a given distribution of power. In his paper, Richards appropriately draws attention to these "lines in the constitutional sand," identifying them as subtle but overarching considerations. I cannot overemphasize that the fundamental issues at stake in constitutionmaking have to do with the drawing of these lines. Only from these fundamentals can the most efficient arrangement of powers emerge. Richards' implicit personal preferences in this regard should be carefully borne in mind.

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[1] We owe to Pareto, the famous nineteenth-century Swiss economist, the rigorous demonstration that any particular allocation of resources among alternative uses can only be characterized as efficient or inefficient if one first takes the existing distribution of wealth as given.

Bureaucracy: The Forgotten Dimension of Power

Constitutions are about power and its uses. While noting this, we should not be slaves to eighteenth-century thinking and to the political philosophers who taught us to identify only three kinds of power: legislative, judicial, and executive. These categories only imperfectly capture the realities of power in modern society — particularly in the constitution of a federal state. What they omit is perhaps the most colossal category of all: bureaucratic power.

Bureaucratic power should not be confused with executive power as defined by the classical political thinkers. In a parliamentary democracy and in a country where the party in power normally commands a parliamentary majority, the classic distinction between executive and legislative powers is not very helpful. The executive power held by elected officials is hardly more than a power to initiate laws. In a parliamentary democracy, real executive authority lies in the hands of unelected officials. One important source of power for these officials lies in the command they have of the information necessary to facilitate the process of governing. Thus far, constitutional debate in Canada has not raised the issue of the vast power wielded by the central bureaucracy.

There is danger in any country where the capital city is isolated from the center of the country's economic and cultural life. The problem is compounded in Canada by the dispersion and diversity of the country's economic and cultural elite. Ottawa is a peculiar city, quite removed both geographically and psychologically from the economic, cultural, and social realities of the country. Thus, divergent and often conflicting concerns can only make their appearance in Ottawa in the guise of sectorial interests. And because they must, in that context, compete for attention, they tend to be perceived as no more than self-seeking lobby groups. It is hard to resist the temptation to mistake an Ottawa perspective for a national one and to refrain from adopting the arrogant mentality that comes naturally with such a view.

Not only is Canada badly governed — as the failures of performance in so many areas over the past few decades bear witness — it is also overgoverned. Comparisons are sometimes made between the number of elected officials here and in California, which has a slightly larger population than Canada and elects far fewer officials. Similar comparison can be made with regard to the number of civil servants in Canada and California. The multiple layers of bureaucracy that have come to denote federalism in this country is one issue that constitutional reform definitely must address.

Although many people in the West and Quebec are willing to concede the case for a substantial and effective set of common rules and practices, that is obscured by their lack of confidence *vis-à-vis* the central bureaucracy. A comparison with the European Community (EC) is instructive. The central EC bureaucracy, the European Commission, has far fewer than 12,000 technocrats for a community of more than 325 million people. This must be contrasted with Canada's more than 250,000 civil servants in a country that is less than one-tenth the size. So far, maintaining Canadian unity seems to have meant making the world safe for the Central Canadian bureaucrats — certainly a less than satisfactory approach.

Significantly, the other essays in this book do not clarify the pivotal distinction between making rules and implementing them. Power, like ownership rights, is almost infinitely divisible and consists of many separate layers that lie together like the layers of an onion. Even with regard to rulemaking, which constitutes just one subdivision of power, one can distinguish the power to initiate, the power to formulate, the delegated power to interpret, the power to regulate, and so on. In Canada, some of the rulemaking powers are exercised by elected officials, but most are in the hands of the bureaucracy. The power to implement rules is also divisible into a large number of different components, all of which belong to bureaucrats.

Examples of multilevel governance in the EC and in federal states such as Germany illustrate the importance of "subsidiarity," a policy by which central governments are only granted jurisdiction over areas that lower levels of government would perform less efficiently. Subsidiarity applies directly to rulemaking power, but it also indirectly ensures that central bureaucrats are granted only a restricted role. In Canada, not only have we failed to recognize bureaucratic power, but, on the contrary, we have permitted the spending power — which is one aspect of the power to implement legislation — to be used to subvert the legislative power distribution contained in the Constitution. This has augmented not only the power of the central government, but, in particular, the power of the central bureaucracy.

The Triple-E (elected, effective, and equal) Senate proposal, much favored by Western public opinion leaders, is an attempt to find a counterweight to the perceived excessive influence of "Central Canada." This term must, however, be subjected to a critical evaluation. The political weight of Ontario and Quebec in Parliament certainly is fairly large, in accordance with their share of elected members, but the centralist mindset of the Ottawa bureaucracy is a much more potent factor. The desire to redress the balance, which has been expressed through the Triple-E proposal, will never be fulfilled unless the influence of the federal bureaucracy is first recognized and curtailed. No one has adequately explained how a few more senators from the West and the Atlantic provinces — especially in the context of a parliamentary government — could have any material impact on the perspectives, the policy formulation, and the legislative and regulatory contributions of the federal bureaucrats. If pushed to its logical conclusion, the Triple-E proposal can only lead to a sacrifice of an effective parliamentary democracy, replacing it with a presidential or a quasi-presidential system, which ultimately would not do anything at all to alter the centralist perspective.

Canada has the potential to survive and prosper, but it will achieve neither unless Ottawa's bureaucratic establishment is first scaled down: the bureaucracy must be humbled; the corporate culture of Ottawa must be overturned. This culture has nurtured divisions among Canada's different regions, bred dependency in some of them, and become essentially inward-looking because of its divorce from the elements of national life that alone could make it viable and relevant. In addition, the bureaucratic culture has an arrogant and colonialist attitude toward Canada's native peoples, again in the interest of asserting and consolidating bureaucratic power.

National Standards in Economic and Social Policy

To function effectively, Canada needs both common policies and common standards. It can be argued persuasively that, for symbolic and historical reasons, certain common policies are necessary to help define Canada's identity as a country, particularly with regard to its southern neighbor, the United States. Leaving these symbolic motives to one side, common policies are still needed to accommodate the existence of the Canadian common market. It is in the individual interest of each province and region to ensure that it competes with the others on a level playing field for jobs and economic prosperity.

These standards and common policies certainly do not have to be all-embracing. On the contrary, the virtue of federalism lies in its flexibility, in its ability to facilitate diversity. To argue for an excessively rigid set of common rules, therefore, would be to cut off one's nose to spite one's face. The point is that some rules are beneficial.

I could present many illustrations in which rulemaking "wars" involving pairs of competitive provinces impoverished both parties. Any intelligent person would readily conclude that the interests of everyone involved would be best served if all agreed to abide by jointly determined decisions. Thus, to produce common rules, all the parties concerned simply need to act in accordance with their own best interests! Indeed, the tendency toward globalization of economic relationships creates an environment of competition at both the national and provincial levels. Despite the absence of any formal coordination mechanism, countries feel compelled, whether they like it or not, to align their fiscal and other policies with those of their neighbors. To deny that reality would be to cripple one's own citizens and businesses, and to stunt the country's ability to prosper. Within a federal country such as Canada, those considerations apply with even greater force. If the Canadian union reflects an enlightened self-interest — as I believe it does — we can be confident that common policies and national standards can emerge for the same reason.

Many Canadians feel, however, that Ottawa pursues national standards and other common rules, not as an expression of the enlightened interest of all provinces and regions of the country, but as a means of asserting and supporting the power of the central bureaucracy. If this view were to be generally accepted, given the present level of esteem and confidence in the central bureaucracy, it would doom any chance for the establishment of a common process for making rules.

Economic union requires many common rules, but also much by way of regional initiative and differentiation. In this age of global economic relationships, the openness of the Canadian economy is far more important than the removal of internal barriers. Insightful students of Canadian economic realities have discerned that the several regions of the country entertain distinct economic relations with various parts of the world. Their competitiveness in these "natural" markets depends more on their ability to discover their particular areas of competitive advantage by region than it does on their ability to develop their competitiveness within the national market. The advocacy of a common market as a basis for international competitiveness is rooted in the outmoded mentality and economics of what Alvin Toffler calls the "second wave": the period of industrialization and mass production, and therefore the period when economies of scale were considered the essential ingredient of competitiveness. In today's world economy, there is no guarantee that economies of scale are a sufficient or even a necessary condition for world competitiveness. The old paradigm that inspired the "National Policy" that Canada instituted shortly after Confederation has been overtaken by events. To the extent that economies of scale remain relevant, the market access that would provide the opportunity for scale may well extend beyond any single country's borders: witness the proliferation of continental regional trading blocks.

At the moment, Ontario is vigorously promoting the concept of a "social charter." There are many ways of looking at this notion. The least acceptable one would picture the social charter as a mere extension of the Charter of Rights and Freedoms, with rules enforceable by the courts and binding on governments. Imagine what this version would entail: governments would be bound forever by rigid rules whose interpretation would rest entirely in the hands of the courts, with no regard for financial constraints and no motivation or ability to innovate or to respond to new ideas and opportunities — in other words, a veritable nightmare.

A more plausible version of a social charter, and one more likely to resemble the Ontario proposal, would be a declaration of principles in the Constitution committing the federal and provincial governments to the adoption of common rules and standards in the area of social rights and benefits. Such a social charter would be a strong invitation to apply to the realm of social policies the approach, previously described, consisting of the voluntary codetermination by the various provinces of common policies and common rules. The self-interest of the provinces (and regions) would be the driving force and a moderating factor. Flexibility would be retained, as well as an ability to innovate and respond to both the ever-changing social and economic context and the shifting interpretation of optimum social rights and benefits.

However, the concept of social charter can have secondary but dangerous implications. Specifically, it can serve as the intellectual basis for the extension of the meddling, busybody tactics of a central bureaucracy preoccupied and consumed by the need to impose its supposedly superior notions of what is right and fair.

The above caveats qualify but do not refute the valid case for common rules in the economic and social domains. The inevitable disappearance of federal grants to the provinces — an evolution that, by itself, is both necessary and desirable — makes such common rules and standards absolutely necessary, especially in areas of provincial jurisdiction.

In order to restore fiscal responsibility, Canadians must bring to an end the era of cost-sharing between governments, in which political sway can be had by the central government at the cost of fifty-cent dollars. It is difficult to believe that cost-sharing has had no role in the bulging deficits at both levels of government. Historically, however, these programs have been the only workable mechanism for coordination between governments in Canada. As I have discussed elsewhere,[2] other approaches have been suggested and attempted, but none, apart from cost-sharing arrangements, has been shown to be effective. Nonetheless, even though it would leave a significant gap in the machinery of government, cost-sharing tactics must be banished in the interest of fiscal responsibility.

To set common rules and national standards, Canada requires a mechanism that reflects the needs and choices of decisionmakers who have operational knowledge of the programs they are trying to harmonize. The empire-builders of the central government should be left out of the process altogether. The following elements are probably all necessary for creating the conditions amenable to the adoption of national standards:

- Control of common rulemaking by those governments that would implement them — that is, the provincial governments.
- A low ceiling on Ottawa's total bureaucracy or, alternatively, a provision to the effect that common rules and national standards would be adopted only in areas where there were no federal involvement whatsoever. After all, it would be logical to consider rules as a *substitute* for, rather than a *complement* to, federal jurisdiction.
- An open agenda for rulemaking that allows provincial governments to develop rules together as they see fit, and allows them

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[2] Claude E. Forget, "The Harmonization of Social Policy," in Mark Krasnick, ed., *Fiscal Federalism*, Collected Research Studies of the Royal Commission on the Economic Union and Development Prospects for Canada 65 (Toronto: University of Toronto Press, 1986), pp. 97–146.

to shape and reshape the rules as needs emerge without any constitutional constraint analogous to a Charter obligation. At most, the Constitution might encourage the creation of such rules by listing areas where they would apply and providing for the rulemaking process itself.

- The elimination of all cost-sharing provisions. The notion of fiscal compensation should become anachronistic. Indeed, in the new fiscal context, the concept of commonly conceived national standards would only be required specifically *because* the federal financing of provincial programs would no longer be an option.
- The requirement of a majority for the adoption of national standards. Conceivably, we could use the "7–50" rule, whereby seven provinces containing 50 percent of the population constitute a majority.
- Judicial enforcement of all collective rules. Rules, once adopted, would create obligations for all provincial governments. Those obligations, inasmuch as they would create entitlements for individuals, should be judicially enforceable.

Setting national standards and common rules of behavior for provincial governments, if one is serious about it, must go beyond the relatively pleasant task of ensuring the free movement of people, goods, and capital. It certainly goes beyond the gratifying role of enforcing the portability of social benefits between provinces. Some hard issues would have to be confronted head on. For instance, whether one considers it a stroke of genius or a disaster, the fiscal year 1991/92 Ontario budget demonstrated that common rules, or at least a common approach, would need to extend to fiscal policy. Only a joint action of provincial governments could guarantee a sound national fiscal policy in Canada. Can the rulemaking guidelines set out above stand such a strain? There is obviously room for considerable doubt on that score: much noise can be expected from the provincial governments concerning their right to respond to their political priorities and the needs of their respective regions. Neither Richards nor Cousineau addresses this issue, which is certainly a neglect.

Dealing with Canada's Inequalities

Without a major reorganization of the Atlantic and Prairie provinces, constitutional evolution in Canada will remain gridlocked. The governments of these provinces continue to seek — through a reorganized but still strong and dominant central government — a solution to their problems. They must come to realize, however, that a real solution, as opposed to a bandage solution, can only be devised at home.

At present, the governments of the Atlantic provinces, as well as those of Manitoba and Saskatchewan, simply do not have the critical mass of citizens and taxpayers necessary to perform adequately. They constitute an exaggerated burden on their respective taxpayers because of the comparatively huge overhead present in virtually every government that serves a population of less than one million. And given their scale and resources, the governments of these provinces simply cannot consistently reach the level of professionalism necessary to be taken seriously. They could, of course, combine their lands, resources, and tax bases into a few larger provinces, but so far they have been unwilling to merge. This has meant that the inefficiency of at least six provincial governments (out of ten) has been imposed on the rest of the country.

Without considering that this situation might be a result of conscious choice, Canadians generally accept this predicament as their fate. The reorganization of Canadian institutions, as described by Richards and Cousineau, may call for extensive decentralization, but such proposals run a high risk of being blocked because they "would not work" in, say, New Brunswick or Manitoba.

Many Canadians advocate a Triple-E Senate in order to bypass the problem of provincial differences. They seek a solution through a reorganization of the central institutions of the country. It is an unfortunate approach. Even if it succeeds in a formal sense, and a Triple-E Senate is achieved, it would only lead to disappointment because, in a democracy, the weight of numbers comes before all and cannot be systematically counteracted. The West's desire to have a better grasp of its own destiny and to gain a greater sense of control over itself cannot be resolved by any modification to Canada's central institutions. It can only be resolved by a decision on the part of the citizens of that region that their regionally elected governments should assume both the power and the responsibility for the region's policies and public services — that is, what can only be achieved through decentralization.

The people living in the Atlantic provinces also look favorably on a strong federal government. There is no need for sophisticated analyses to understand why: this is where the money comes from.

Here, again, is a large element of self-delusion. No matter what some parties may believe, the appetite for equality in Canada is actually quite limited, especially on the part of the traditional net contributors. This country has the amazing distinction of having turned a mechanism designed to promote national harmony into the greatest single source of acrimony and mutual distrust in its history. Double-entry bookkeeping has now become universal practice in every Canadian region. Everyone, as a result, has become acutely sensitive to their respective advantages and disadvantages or, more concretely, to the "benefits" and "costs" involved in belonging to the Canadian federation. Not surprisingly, from a regional perspective, every one of these cost-benefit accounts look disappointing. Notwithstanding that every single government in Canada now finances benefits for its citizens widely in excess of the taxes it takes in, citizens all over the country feel cheated and can quote detailed studies and extensive sets of figures to "prove it"! Equalization, and other redistribution programs, are as large as they ever will be. But the ability of Canada as a whole to tap economic rents in order to subsidize its poorer area has lessened drastically of late. By all accounts, we can no longer consider economic rents from the exploitation and exportation of natural resources to be the rich sources they once were. In the competitive atmosphere of the 1990s, Canada's sluggish productivity growth has finally begun to make itself felt. Consequently, Ontario, as a source of "surplus" wealth, has been rapidly cut down to size.

Section 36 of the Constitution now guarantees the principle of equalization, so there is no doubt that the principle will continue to be honored. However, the way we implement this principle will become more and more crucial to its acceptability. The simple-minded notion that a strong central institution in Ottawa can ensure the uninterrupted flow of equalization payments is self-deception on the same scale as the Triple-E concept. Open-ended equalization, with no strings attached, not only subsidizes public services delivered to the citizens of the poorer areas of the country; in effect, it also subsidizes inefficient provincial government overhead and inflationary public service pay levels. Canadians harbor a widely felt moral duty to finance a fairly high level of services countrywide in the fields of education and health. This generosity is, in fact, well supported by efficiency arguments. But one would be dreaming to imagine that Canadian taxpayers, particularly in the more difficult days that lie ahead, will continue to underwrite inefficient programs. For instance, why should taxpayers continue to support a labor market policy that condones an extraordinarily inept combination of unemployment insurance and ineffective make-work projects whose only rationale is to trigger entitlements to further social benefits?

There *are* other options. In the Atlantic provinces, where most of these considerations apply with special force, a solution lies in greater regional autonomy and self-determination. This cannot be acquired through transfer payments, which are controlled by the central bureaucracy. Instead, I can envision section 36 being implemented by means of equalization accounts set up to accommodate the differentials in regional per capita gross domestic product. This would grant total control to the provinces. To such an account would be debited not only the subsidies for public services such as education and health care but also the cost of all other programs targeted at regional disparities through labor force training, job creation, wage subsidies, and special social allowances. In a country with waning natural resource rents and persistent productivity problems, generosity and solidarity will have to acquire a new and more constrained meaning. However, the beneficiary regions would probably improve their lots by making the required tradeoff themselves, rather than entrusting this function to a distant, uninterested bureaucracy.

Some would go even further: Cousineau even suggests that the center be granted no role at all in social security matters. Such a radical proposal glosses over a number of difficulties. The first and most important problem is that, within any scenario, the central government will continue to levy a personal income tax. Notions belonging to the field of social security have long been implicit and even explicit in the operation and design of all personal income tax regimes: personal and family-based exemptions, tax credits, and rules governing the allowability of certain "social" personal expenditures, such as health services, day care for children and assistance in the home for the handicapped or the elderly, have at all times and in all countries made the personal income tax a significant instrument of social policy. Existing proposals to integrate social welfare transfers to families and individuals into the personal income tax scheme, under the authority of a "negative income tax," would further enhance that role. The tax credit granted in connection with the goods and services tax is a perfect example of a negative extension of the personal income tax. Old age security pensions and family allowances could both be transformed quite easily to this format.[3]

This breach in the wall that keeps social policy under the exclusive jurisdiction of the provinces does not leave much of the wall standing. But there is a further complication. Commitments by Canadians to unencumbered distribution of equalization payments is tenuous at best. But Canadians would never accept that provincial or regional governments that receive equalization transfers should be able to distribute them according to their own priorities, social values, and preferences. The absolute, unquestioning commitment to horizontal equity among Canadians simply does not exist. There is no doubt that provinces should have greater responsibility in deciding how equalization funds should be divided among competing interests. This is desirable in order to improve the efficiency with which these funds are spent. But it would be unrealistic to suggest that their choices should be completely unrestricted. The creation of an equalization account, as suggested above, would certainly constitute a primary area for the development of national standards.

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[3] This was written before the contents of the 1992 federal budget were known.

Quebec has already seen the wisdom of such a compromise. At in the 1971 Victoria conference on the Constitution, Quebec insisted on provincial supremacy in the field of social security. Nearly ten years later, in the Beige Paper, the Quebec Liberal Party implicitly acknowledged that this demand had been a mistake.[4] Then, largely for the above-mentioned reasons, it limited its claim to supremacy to health and social services but not to the entire area designated under the label of social security.

Conclusion

How much change can Canada reasonably absorb at this point in its evolution? The recommendations emerging from this and other studies are both numerous and complex. Should we not attempt to focus on a few essential ingredients of change? The current insistence on popular involvement and, ultimately, sanction through a referendum, or referenda, militates strongly in favor of simplicity.

In that spirit, I would venture to make the following suggestion: impose, by a constitutional amendment, a cap on the central bureaucracy, and set this cap at a low figure of, say, 25,000 persons — excluding the Armed Forces and industrial-type public services such as Canada Post Corporation and Via Rail. Then, mandate that the reduction to the desired level takes place over a short period — say, four years — and place a moratorium on all the constitutional issues now being hotly debated, ranging from the "distinct society" to a Triple-E Senate!

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[4] Quebec Liberal Party, Constitutional Committee *A New Canadian Federation* (Quebec, 1980).

To rein in the central bureaucracy by means of mandatory reduction has immense potential for changing the way in which power is exercised, not only centrally but in the provinces as well. As a consequence, the very process of policymaking and the nature of political expectations would alter so much that I believe the issues we have set aside might never be taken up again, since the need for change that inspired them in the first place would have already been satisfied.

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Claude E. Forget has had a career spanning academia, provincial public administration and politics, and the private sector. He came to social policymaking from the perspective of economics and, in the 1970s. was responsible for devising and/or implementing several of the financial and organizational features of health and social services in Quebec concomitant with the introduction of medicare. In that role and later, at the time of the 1980 Quebec referendum, he was extensively involved in federal-provincial and constitutional affairs. in 1985–86, he chaired the federal Commission of Inquiry on Unemployment Insurance.

John Richards grew up in Saskatchewan and served as a member of that province's legislature during the first term of the Blakeney government from 1971 to 1975. For the first two years of his term, he was legislative secretary to the Minister of Health. In mid-term, he crossed the floor and sat as an "independent socialist." In his words, he has "since mellowed and rejoined the NDP." Trained as an economist, he currently teaches in the business faculty at Simon Fraser University, Burnaby, B.C. He has written on resource policy, labor relations, and public policy.

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